



THE APPRAISAL FOUNDATION
*Authorized by Congress as the Source of Appraisal
Standards and Appraiser Qualifications*

National Uniform Standards of Professional Appraisal Practice (USPAP) Course

Student Manual
15-Hour Course

Reviewed and Updated By

The Appraisal Standards Board (ASB)

In Cooperation With

The Education Council of Appraisal Foundation Sponsors (ECAFS)

Approved By

The Appraiser Qualifications Board (AQB) through its Course Approval Program

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Title XI: Real Estate Appraisal Reform Amendments

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Appendix III

OMB Bulletin No. 92-06
OMB (Office of Management and Budget) Circular A-129, revised November 29, 2000

Appendix IV

Suggested Responses to Discussion Examples (may be packaged separately)

NOTE: Each student must also have a copy of the *Uniform Standards of Professional Appraisal Practice (USPAP) 2005* (effective January 1, 2005).

The course sponsor may include additional materials.



THE APPRAISAL FOUNDATION

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STUDENT TRACKING FORM

Please complete the information below and return this *original form* to the Instructor at the end of the course. Completion of this form is required in order to receive a *Course Completion Verification Form* from The Appraisal Foundation.

Please **PRINT** the following information (incomplete or illegible forms will not be processed):

Course Name: 2005 15-Hour National USPAP Course or its equivalent

Course Dates and Location _____

Instructor Name _____

Course Provider _____

Student Name _____ SSN# XXX-XX-
(last 4 digits only)

Street Address _____

City/State/Zip _____

Phone _____

Email _____

INSTRUCTOR VERIFICATION – This section to be completed by the Instructor.

I hereby certify that the student listed above completed the following:

15-Hour National USPAP Course (**with examination**) *15HR05*

Passed Failed Exam Re-take

OR

15-Hour National USPAP Course (**no examination**) *15HR05-NE*

This course was offered via: Classroom **OR** Distance Education (online, CD, etc.)

Instructor ID# _____ **State Certified Appraiser -** Yes **or** No
(As provided by The Appraisal Foundation)

Signature (required)

Date



THE APPRAISAL FOUNDATION

*Authorized by Congress as the Source of Appraisal
Standards and Appraiser Qualifications*

1029 Vermont Avenue, NW, Suite 900, Washington, DC 20005

Tel: (202) 347-7722—Fax: (202) 347-7727

www.appraisalfoundation.org

SPONSORING ORGANIZATIONS OF THE APPRAISAL FOUNDATION:



American Society of Appraisers

703-478-2228

www.appraisers.org



American Society of Farm Managers & Rural Appraisers

303-758-3513

www.asfmra.org



Appraisal Institute

312-335-4100

www.appraisalinstitute.org



International Association of Assessing Officers

312-819-6100

www.iaao.org



International Right of Way Association

310-538-0233

www.irwaonline.org



Massachusetts Board of Real Estate Appraisers

781-329-1996

www.mbre.org



National Association of Independent Fee Appraisers

314-781-6688

www.naifa.com



National Association of Master Appraisers

800-229-6262

www.masterappraisers.org

National USPAP Course, 15-Hour

COURSE DESCRIPTION

The National Uniform Standards of Professional Appraisal Practice (USPAP) Course, 15-Hour Course (hereafter referred to as the National USPAP Course, 15-Hour) of The Appraisal Foundation focuses on the requirements for ethical behavior and competent performance by appraisers that are set forth in the *Uniform Standards of Professional Appraisal Practice* (USPAP). This course is unique in that it was developed in 1998 and is revised annually for The Appraisal Foundation with assistance from the Education Council of Appraisal Foundation Sponsors (ECAFS).

Each student must also have a copy of the current *Uniform Standards of Professional Appraisal Practice* document, which provides the framework for the course and is referred to throughout the course. It is important that participants become familiar with this document.

The course material emphasizes the role of the appraiser and the impartiality associated with this role. The special responsibilities of the appraiser with regard to impartiality are explored in detail.

In addition to lectures, the course includes Discussion Examples that show how USPAP applies to situations that appraisers encounter in everyday practice. These examples address issues frequently experienced by appraisers as professionals in the appraisal of real property, personal property, and businesses or intangible assets; in appraisal review; and in real property appraisal consulting assignments.

This course is designed to aid appraisers in all areas of appraisal practice seeking competency in USPAP, including those subject to state licensing or certification and continuing education requirements imposed by professional organizations, client groups, or employers.

The *Uniform Standards of Professional Appraisal Practice* have been endorsed and adopted by major appraisal organizations of the United States and Canada. As required by federal law, USPAP must be used by states in their real estate appraiser certification programs.

This course provides at least 15 hours (50 minutes/hour) of instruction in USPAP and allows for a one-hour exam period.

Course Materials

In addition to this Student Manual, participants must also have the current edition of the *Uniform Standards of Professional Appraisal Practice*. The Suggested Responses to Discussion Examples may be packaged with the Student Manual or distributed separately. The course sponsor may provide additional materials.

The Student Manual includes the following:

1. Course description
2. Course schedule
3. Lesson objectives for each lecture

4. Lecture outlines, which include Discussion Examples
5. Appendix I: Title XI: Real Estate Appraisal Reform Amendments
6. Appendix II: Independent Appraisal Evaluation Functions and OCC Bulletin: Interagency Appraisal and Evaluation Guidelines
7. Appendix III: OMB Bulletin No. 92-06 and OMB Circular A-129
8. Appendix IV: Suggested Responses to Discussion Examples

Course description. The course description summarizes the course and highlights major topics.

Course outline. The course outline lists the lecture titles and associated parts of USPAP to be covered in each section. Although there are many topics to cover, the course has been designed to provide ample opportunity to master the appropriate material. Completing the reading assignments before each session will help you to become familiar with the concepts that will be presented. Discussion Examples will help you to understand application of the concepts taught. The course review offers an opportunity to clear up any problems you may have with the material.

Lesson objectives. Learning goals have been established for each section. These objectives may be cross-referenced to the lectures and/or USPAP. Familiarize yourself with the lesson objectives before you read each section outline and the applicable parts of USPAP; they will alert you to the important topics to be mastered. By reviewing these objectives after the assigned reading and again after the class presentation, you will be able to gauge whether you have understood key points.

Lecture outlines. Outline entries broadly identify the content to be mastered. All direct quotations from USPAP, as well as USPAP terminology items, appear in *italic* type. If possible, read and study each lecture outline and the appropriate section of USPAP before the appropriate session so you will be prepared to participate in the class discussion and ask meaningful questions.

Course Review

Section J is devoted to a review of the course, which will be your final opportunity to ask questions about any topics that have presented difficulty. Instructors may conduct the review by going over the lesson objectives, highlighting outline topics, and/or reviewing Discussion Examples.

Prepare for this section by reviewing all the course material. Know ahead of time what you want to get out of this review, and be sure to ask questions. Be especially attentive to the discussion of course topics that you have found difficult.

Examination

The one-hour, multiple-choice exam consists of 50 questions. You will be required to recognize definitions and concepts presented in the course, but not to memorize all of the Standards Rules.

Examination Requirement

A final examination is required for students who are taking this course to fulfill their USPAP qualifying education requirement.

Students who are taking this course to fulfill their USPAP continuing education requirement should be aware that some state appraisal licensing boards may not require the student to take and pass the examination in order to receive credit. It is up to the student to determine his or her state's requirements in terms of examinations and how many hours are awarded if the examination is not taken or if the examinee fails to pass.

NOTE: The instructor(s) will provide directions for completing any forms that are necessary for the presentation and record keeping of this course.

Complaint Process

For the protection of all parties, The Appraisal Foundation has set up procedures for processing student complaints under the AQB Certified USPAP Instructor Program.

The complaint must be provided in writing to The Appraisal Foundation. The complaint will be reviewed to determine whether it has merit. If it is determined that the complaint has merit, an investigation will be conducted followed by a recommendation as to the next course of action.

COURSE OUTLINE

Orientation

Introduction

Explanation of Course

Explanation of Student Manual and Additional Materials

Explanation of Course Procedures

Ground Rules

Questions

Suggested Timetable

Section A

History, Professionalism, Valuation Services and Appraisal Practice, and the PREAMBLE and Structure of the *Uniform Standards of Professional Appraisal Practice*

History

Professionalism

Valuation Services and Appraisal Practice

Structure of USPAP

The Structure of USPAP Related to the Appraisal Process

The Scope of Work Decision—Introduction

The Statements—Introduction

The Advisory Opinions (Guidance Material)—Introduction

As guidance material, selected Advisory Opinions (AOs)¹

Guidance:	AO-21:	<i>USPAP Compliance</i>
	AO-25:	<i>Clarification of the Client in a Federally Related Transaction</i>

Section B

Uniform Standards of Professional Appraisal Practice: DEFINITIONS and Rules

Selected Statements on Appraisal Standards (SMTs), and, as guidance material, selected Advisory Opinions (AOs)

DEFINITIONS

ETHICS RULE

SMT-9: *Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions*

Guidance: AO-25: *Clarification of the Client in a Federally Related Transaction*

AO-27: *Appraising the Same Property for a New Client*

COMPETENCY RULE

Guidance: AO-9: *The Appraisal of Real Property That May Be Impacted by Environmental Contamination*

AO-13: *Performing Evaluations of Real Property Collateral to Conform with USPAP*

AO-14: *Appraisals for Subsidized Housing*

DEPARTURE RULE

SMT-7: *Permitted Departure from Specific Requirements in Real Property and Personal Property Appraisal Assignments*

Guidance: AO-15: *Using the DEPARTURE RULE in Developing a Limited Appraisal*

1. Statements on Appraisal Standards (SMTs) and Advisory Opinions (AOs) may be addressed, as appropriate, in various sections of the course. Other cross-references to the USPAP document are also noted where applicable.

JURISDICTIONAL EXCEPTION RULE

SUPPLEMENTAL STANDARDS RULE

- SMT-10: *Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction*
- Guidance: AO-25: *Clarification of the Client in a Federally Related Transaction*

Section C

Uniform Standards of Professional Appraisal Practice:
STANDARD 1—Real Property Appraisal, Development

- SMT-2: *Discounted Cash Flow Analysis*
- SMT-3: *Retrospective Value Opinions*
- SMT-4: *Prospective Value Opinions*
- SMT-6: *Reasonable Exposure Time in Real Property and Personal Property Market Value Opinions*
- SMT-9: *Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions*
- SMT-10: *Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction*
- Guidance: AO-1: *Sales History*
- AO-2: *Inspection of Subject Property Real Estate*
- AO-3: *Update of a Prior Assignment*
- AO-4: *Standards Rule 1-5(b)*
- AO-7: *Marketing Time Opinions*
- AO-8: *Market Value vs. Fair Value in Real Property Appraisals*
- AO-17: *Appraisals of Real Property with Proposed Improvements*
- AO-18: *Use of an Automated Valuation Model (AVM)*

- AO-19: *Unacceptable Assignment Conditions in Real Property Appraisal Assignments*
- AO-22: *Scope of Work in Market Value Appraisal Assignments, Real Property*
- AO-23: *Identifying the Relevant Characteristics of the Subject Property of a Real Property Appraisal Assignment*
- AO-24: *Normal Course of Business*
- AO-25: *Clarification of the Client in a Federally Related Transaction*
- AO-27: *Appraising the Same Property for a New Client*

Uniform Standards of Professional Appraisal Practice:
STANDARD 2—Real Property Appraisal, Reporting

- Guidance: AO-5: *Assistance in the Preparation of an Appraisal*
- AO-11: *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*
- AO-12: *Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2*
- AO-16: *Fair Housing Laws and Appraisal Report Content*
- AO-26: *Readdressing (Transferring) a Report to Another Party*

Section D

Uniform Standards of Professional Appraisal Practice:
STANDARD 3—Appraisal Review, Development and Reporting

- Guidance: AO-20: *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*

Section E

Uniform Standards of Professional Appraisal Practice:
STANDARD 4—Real Property Appraisal Consulting, Development

Uniform Standards of Professional Appraisal Practice:
STANDARD 5—Real Property Appraisal Consulting, Reporting

Guidance: AO-21: *USPAP Compliance*

Section F

Uniform Standards of Professional Appraisal Practice:
STANDARD 6—Mass Appraisal, Development and Reporting

Section G

Uniform Standards of Professional Appraisal Practice:
STANDARD 7—Personal Property Appraisal, Development

Uniform Standards of Professional Appraisal Practice:
STANDARD 8—Personal Property Appraisal, Reporting

Guidance: AO-11: *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*

AO-12: *Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2*

Section H

Uniform Standards of Professional Appraisal Practice:
STANDARD 9—Business Appraisal, Development

Uniform Standards of Professional Appraisal Practice:
STANDARD 10—Business Appraisal, Reporting

Section I

Statements on Appraisal Standards and Advisory Opinions

Section J

Course Review

ORIENTATION

I. Introduction

- A. Instructors
- B. Staff
- C. Facilities

II. Explanation of Course

- A. Course objectives
- B. Place of course in State Regulatory System

III. Explanation of Student Manual and Additional Materials

- A. Course description
- B. Course schedule
- C. Lesson objectives for each lecture cross-referenced to lectures and, where appropriate, to USPAP
- D. Lesson outlines
- E. Discussion Examples
- F. Appendix I
Title XI: Real Estate Appraisal Reform Amendments
- G. Appendix II
Independent Appraisal and Evaluation Functions and OCC Bulletin: Interagency Appraisal and Evaluation Guidelines
- H. Appendix III
OMB Bulletin No. 92-06 and OMB Circular A-129

- I. Appendix IV
Suggested Responses to Discussion Examples (may be provided under separate cover)
- J. *Uniform Standards of Professional Appraisal Practice*, current edition (student must have)

IV. Explanation of Course Procedures

- A. Evaluations
- B. Time schedule
 - 1. Coffee breaks
 - 2. Lunch breaks
- C. Attendance
- D. Class discussions
- E. Additional assistance
- F. Examination
 - 1. Time
 - 2. Place
 - 3. Administrative procedures

V. Ground Rules

- A. Taping equipment
- B. Other credit for this course

VI. Questions

**SUGGESTED TIMETABLE
(TO MEET STATE REAL ESTATE APPRAISAL REGULATORY
REQUIREMENTS)**

**NATIONAL UNIFORM STANDARDS OF PROFESSIONAL
APPRAISAL PRACTICE (USPAP) COURSE
15-HOUR COURSE**

Day 1

8:00 a.m. Orientation

Section A – History, Professionalism, Valuation Services
and Appraisal Practice, and the PREAMBLE and
Structure of the *Uniform Standards of Professional
Appraisal Practice* (USPAP)

Section B – DEFINITIONS and Rules

11:30 – 12:30 p.m. Lunch

Section B Continued

Section C – STANDARD 1

Day 2

8:00 a.m. Section C – STANDARD 2

Section D – STANDARD 3

Section E – STANDARDS 4 and 5

11:30 a.m. – 12:30 p.m. Lunch

Section E – Continued

Section F – STANDARD 6

Sections G and H – STANDARDS 7–10

Sections I and J – Statements, Advisory Opinions, and Review

This is a suggested teaching schedule. State Appraiser Board approval may be necessary when this course is presented to real estate appraisal practitioners seeking education credit for state licensing or certification–related use. If such approval is required, some modification to this schedule may be required.

END OF SECTION



SECTION A

History, Professionalism, Valuation Services and Appraisal Practice, and the PREAMBLE and Structure of the *Uniform Standards of Professional Appraisal Practice* (USPAP)

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the history of the development of the appraisal profession and the *Uniform Standards of Professional Appraisal Practice*. See I.
- Understand the importance of maintaining “public trust” in appraisal services. See I.
- Recognize the importance of professionalism. See II.
- Recognize the scope of appraisal practice covered by USPAP. See III.
- Identify the structure of the *Uniform Standards of Professional Appraisal Practice*. See IV, A.
- Recognize the relationship between the organization of USPAP (as described in the PREAMBLE) and the essential steps in the appraisal process. See IV, B.
- Recognize the significance of the scope of work decision and the appraiser’s responsibility for that decision. See IV, B, 2.
- Recognize the significance of Statements on Appraisal Standards and review the titles of the Statements currently in effect. See IV, C.
- Recognize the significance of Advisory Opinions and review the titles of the Advisory Opinions currently in effect. See IV, D.

History, Professionalism, Valuation Services and Appraisal Practice, and the PREAMBLE and Structure of the *Uniform Standards of Professional Appraisal Practice (USPAP)*

The definitions of the following terms should be reviewed in relation to this section:

Appraisal Practice

Appraiser

Client

Intended Use

Intended User

Scope of Work

Valuation Services

The Appraisal Standards Board periodically issues Statements on Appraisal Standards (SMTs) and Advisory Opinions (AOs). The following Advisory Opinions should be studied in conjunction with this section:

Guidance:

- AO-21: *USPAP Compliance*
- AO-25: *Clarification of the Client in a Federally Related Transaction*

I. History

The history of the development of the appraisal profession and the *Uniform Standards of Professional Appraisal Practice*

A. The role of the appraiser in society

- Appraisal practice has been in a state of evolution.
- Organized groups of professional appraisers began to appear in the U.S. in the 1930s, largely as a result of the financial chaos of the 1920–30s era.
- Episodes of turmoil and abuse of the appraisal process again appeared in the 1950s, 60s, and 70s, climaxing with the “Savings and Loan (S&L) Crisis.”

- By the 1960s, professional organizations were providing education programs and working to foster greater public recognition and trust in the work of their members.
- Fostering public trust in the work of their professional members was an important part of the organizations' activities.
- These organizations realized that:
 1. Providing credible appraisal services is necessary to the general economic well being of society.
 2. A genuine social need exists for appraisal services by ethical and competent individuals.
 3. Such services created a sense of "trust" in the appraiser and in professional appraisal practice.

B. The development of appraisal standards

- Leaders of professional appraisal organizations saw the need for a common set of professional practice standards and enforcement of those standards.
- Their initial work focused on agreeing to a common definition of market value for use in real estate appraisals prepared for use by lenders.
- Eight U.S.-based organizations and the Appraisal Institute of Canada formed a committee to develop what was to become, in January 1989, the *Uniform Standards of Professional Appraisal Practice* (USPAP).
- This group recognized that establishing public recognition and acceptance of the resulting standards would require a new organization.
- This new organization would have independent authority over the standards and place the public's benefit ahead of any other constituency, including the membership of the professional appraisal organizations.
- In 1987, eight major U.S. professional appraisal organizations established The Appraisal Foundation (TAF) including:
 1. The Board of Trustees (BOT),
 2. The Appraisal Standards Board (ASB), and
 3. The Appraiser Qualifications Board (AQB).
- TAF constituted these Boards with the exclusive authority to promulgate the standards and qualifications criteria for the benefit of the public, without preference to any constituency.

- USPAP was created with the expressed purpose of promoting and preserving public trust and confidence in professional appraisal practice.
- Different asset types are appraised, but all under one profession—the appraisal profession—so all appraisal disciplines were included in USPAP.
- Public acceptance of USPAP and The Appraisal Foundation came from a variety of actions that collectively established USPAP as the generally recognized appraisal standards for use when the public’s trust was at stake:
 1. Congress recognized USPAP as *the generally recognized standards of practice in the appraisal profession*.
 2. Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) provided recognition and authorized federal financial institution regulatory agencies to reference USPAP in their regulations.
 3. The Executive Branch followed Congress by referencing USPAP in the Uniform Relocation Assistance and Real Property Acquisition Policies Act (the Uniform Act).
 4. With the Office of Management and Budget (OMB) Circular A-129, dated January 11, 1993, other federal agencies recognized USPAP.
 5. Private industry groups such as Fannie Mae, Freddie Mac, Farmer Mac, and the Employee Relocation Council referenced USPAP and integrated the standards in their policies.
- Today, this commitment to fostering greater trust and confidence in professional appraisal practice is the task of the ASB and AQB in cooperation with the sponsoring organizations of The Appraisal Foundation.
- Contained within this notion of “trust” is a relationship that requires the professional to provide more than skill or expertise:
 1. There is a distinct ethical obligation to act in behalf of the public interest, not out of self-interest.
 2. Precisely because of the public interest aspect of the service, the public has a need to be able to trust that a professional will act in an ethical and competent manner.
 3. Appraisers, much like accountants and physicians, are expected to provide their services in an independent, objective, and

impartial manner without preference or accommodation of personal interests toward either themselves or those they serve.

C. The Appraisal Foundation (TAF), BOT, ASB, and AQB

- The Appraisal Foundation (TAF) is not a government agency, nor is it a professional organization with individual members. It is a non-profit, private organization, established for educational and scientific purposes.
- In addition to its own Board of Trustees (BOT) and its two independent Boards, the ASB and AQB, The Appraisal Foundation includes three advisory councils: TAFAC (The Appraisal Foundation Advisory Council), IAC (Industry Advisory Council), and ECAFS (Education Council of Appraisal Foundation Sponsors).
- The Board of Trustees (BOT) exercises all authority and power and performs all functions of The Appraisal Foundation, except for the authority, powers, and functions that the Articles of Incorporation or the Bylaws have directed or required to be exercised or performed by the Appraisal Standards Board or the Appraiser Qualifications Board. The BOT has two primary functions: to appoint members to the ASB and AQB, and to ensure financing of TAF.
- The Appraisal Standards Board (ASB) exercises all authority and power over the subject, style, content, and substance of USPAP and its other communications and performs all functions of the Foundation and the Board of Trustees with respect to establishing, improving, and promulgating *Uniform Standards of Professional Appraisal Practice* and ethics.
 1. USPAP establishes standards of professional appraisal practice for the guidance and education of appraisers, the users of appraisals, government agencies, regulatory bodies, financial institutions, investors, real estate brokers, issuers of securities, and the general public.
 2. USPAP includes the DEFINITIONS, PREAMBLE, Rules, Standards Rules, Comments, and Statements.
 3. Guidance—in the form of Advisory Opinions and an Index—is also provided in the same bound publication for convenience. These items are examples of “other communications” that the ASB may issue regarding USPAP but they do not purport to be USPAP.
 - a. Monthly Q&As are available on The Appraisal Foundation’s website at www.appraisalfoundation.org. These are compiled annually into the *Frequently Asked Questions* (FAQ) publication that is available for purchase from The Appraisal Foundation.

b. Some changes made to USPAP by the ASB have been the result of unsolicited letters or responses to exposure drafts from a variety of sources, including appraisal organizations, government agencies, client groups, work groups, appraisers, and private individuals.

c. In reviewing comment letters received on exposure drafts, the ASB focuses on the reasoning and insight presented in the letter, rather than the source or authorship. The Board's obligation in this process is to the good of the profession and to the public who rely on professional appraisal services.

- The Appraiser Qualifications Board (AQB) exercises all authority over the establishment of education, experience, and other criteria for licensing, certification, and recertification of qualified appraisers by defining, issuing, and promoting such qualification criteria, and disseminating such qualification criteria to states, governmental entities, and others.

D. Legal authority and the adoption process

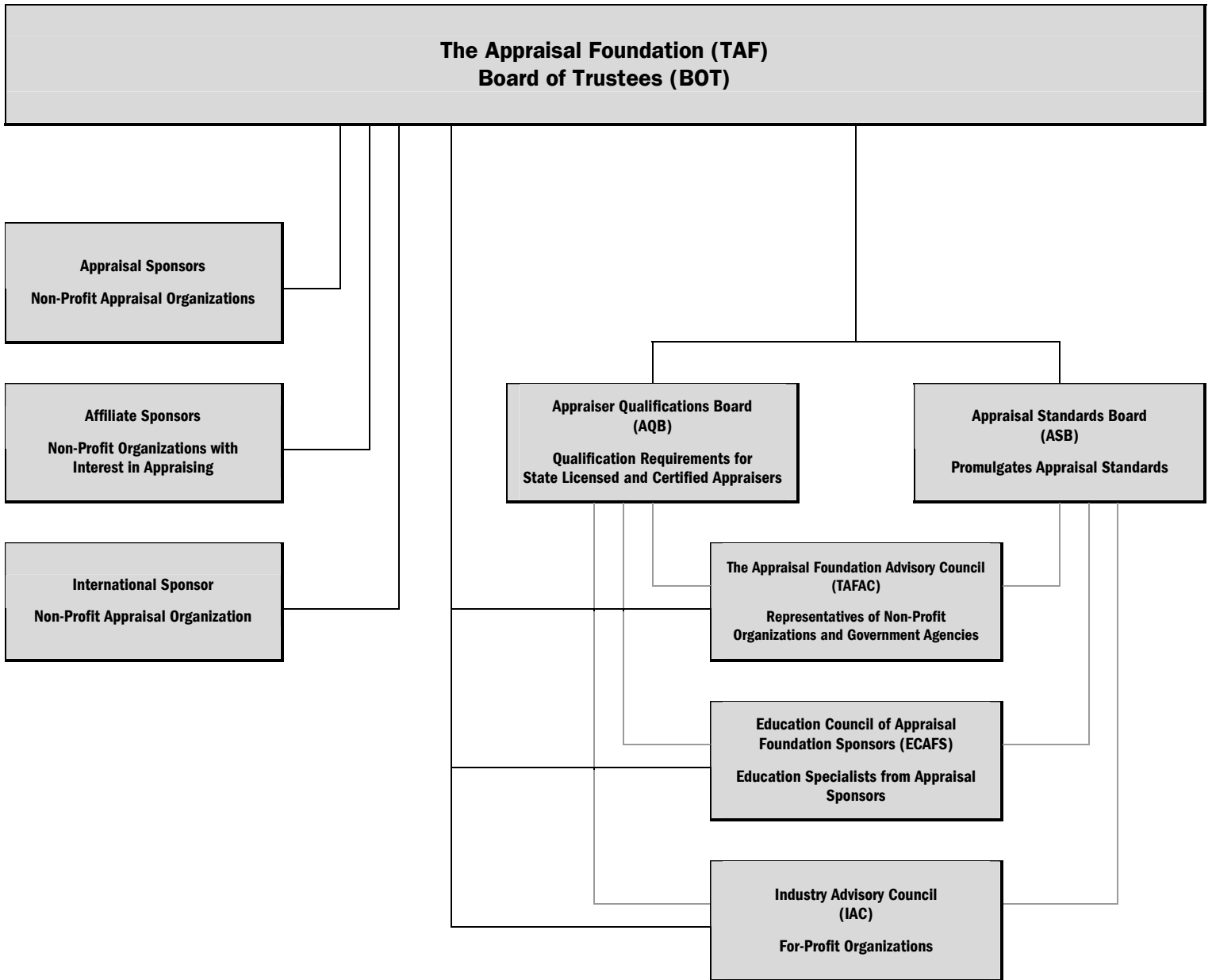
- The Appraisal Foundation is a private entity, not a government agency; and neither The Appraisal Foundation nor its Boards have legal authority in any jurisdiction.
- USPAP achieves legal authority by adoption, citation, or implementation by government agencies through regulation or administrative actions, or by private enterprise in the form of their standards or contract requirements.

E. The Appraisal Subcommittee (ASC)

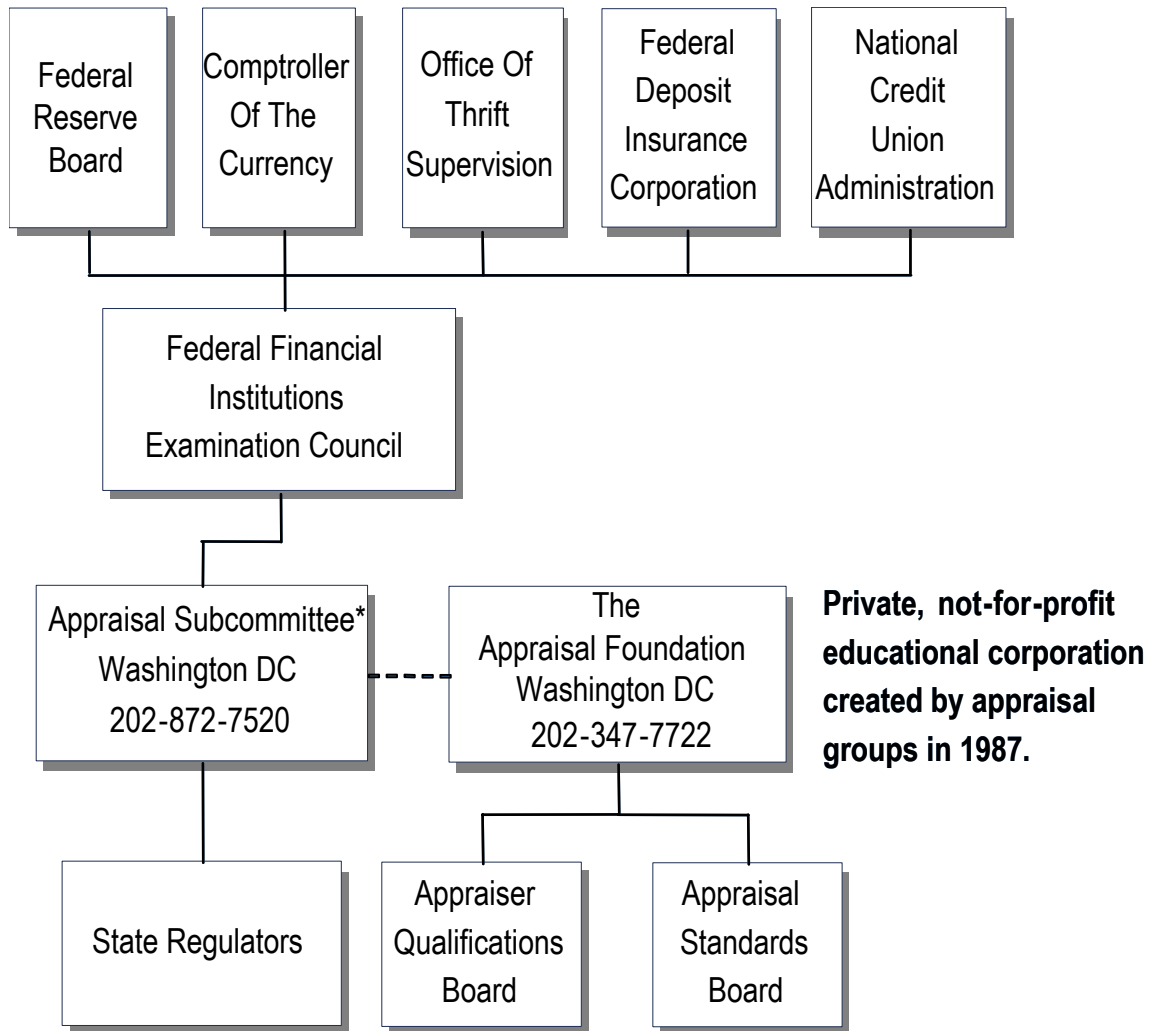
- The ASC's mission is to ensure that real estate appraisers who perform appraisals in real estate transactions that could expose the United States government to financial loss are sufficiently trained and tested to ensure competency and independent judgment according to uniform professional standards and ethics.
- Although not a part of The Appraisal Foundation, the ASC has authority from Title XI to oversee the activities of TAF, including both the ASB and the AQB.
- Title XI also authorized the ASC to oversee the activities of state appraisal agencies.
- The ASC makes an annual report to Congress.

- All ASC operations are funded by state certified or licensed appraisers, each of whom currently pays an annual National Registry fee to the states, which then pay it to the ASC.
- The ASC manages grants to The Appraisal Foundation that are used to support, in part, the real property–related work of the ASB and the AQB.

The Appraisal Foundation General Relationships



FIRREA Relationships



*** Consists of the five banking agencies and HUD**

Legend of Terms

The Board of Trustees (BOT)

The Appraisal Foundation Advisory Council (TAFAC)

The Industry Advisory Council (IAC)

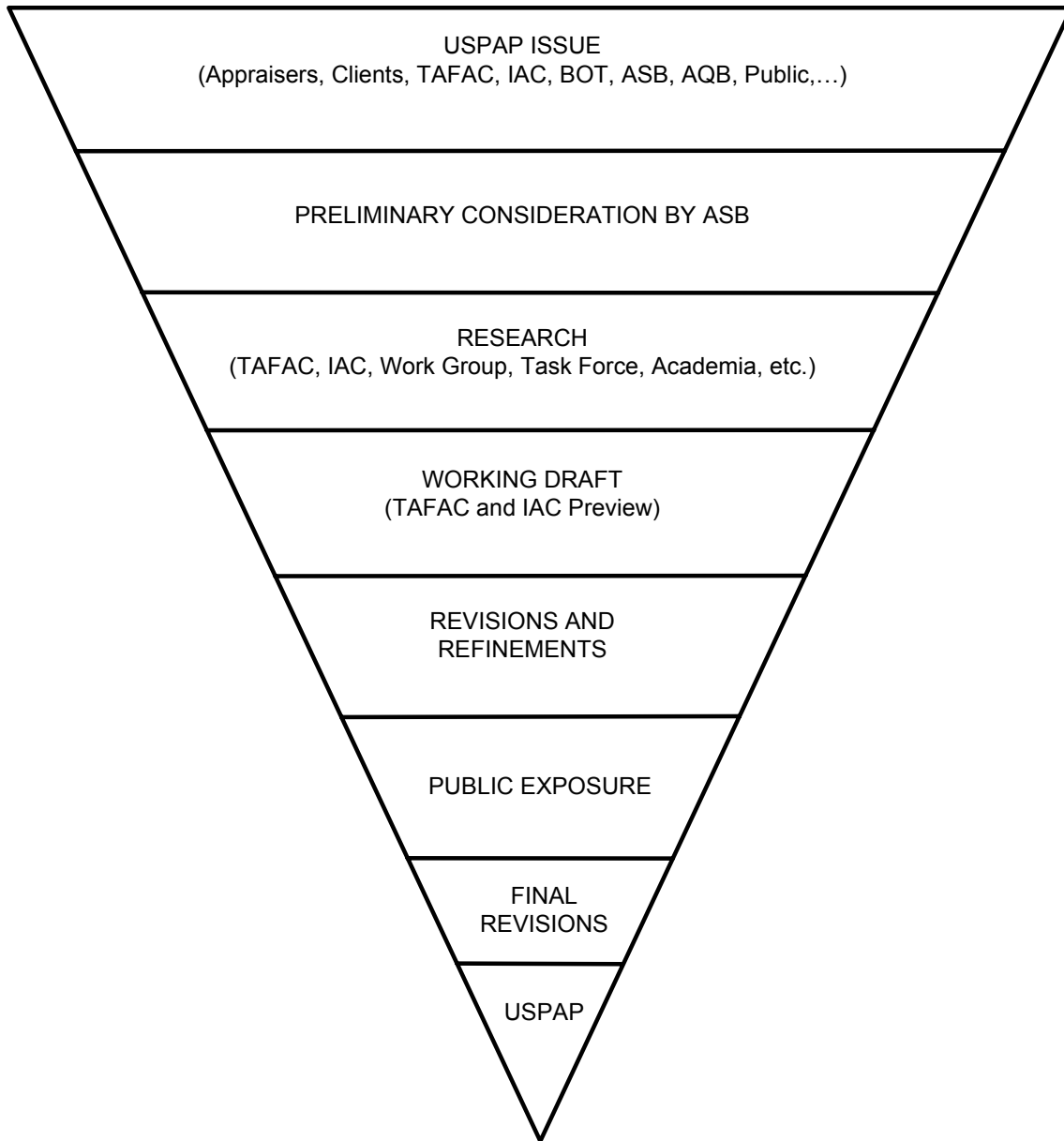
The Education Council of Appraisal Foundation Sponsors (ECAFS)

Appraisal Standards Board (ASB)

Appraiser Qualifications Board (AQB)

The Appraisal Subcommittee (ASC)

How the ASB Develops USPAP



II. Professionalism

Within USPAP, issues of professionalism focus on two areas, ethics and competency. In order to generate and maintain public trust in the profession of appraisal, which is necessary for the smooth flow of the economy, appraisers must perform ethically and must be competent to provide the service they are offering.

- A. A profession, as distinguished in law from a trade, is a vocation calling for all four elements listed:
 - 1. Predominantly mental and intellectual labor and skill
 - 2. Education and special knowledge implying professional attainments
 - 3. Standards of practice to be understood and observed
 - 4. Observation of the standards of practice to be monitored by some type of enforcement

- B. The extent of professionalism by a practitioner in any profession (law, medicine, appraising, etc.) is measured by:
 - 1. The competence and expertise demonstrated
 - 2. The thoroughness of the description documented
 - 3. The quality of the information and process used to reach a conclusion
 - 4. The soundness of the conclusions reached

NOTE: See the definitions below from *Black's Law Dictionary*. The National Labor Relations Act provides additional information on characteristics of a profession or a professional.

Profession: 1. *n.* A vocation requiring advanced education and training.
2. Collectively, the members of such a vocation.

Professional: *n.* A person who belongs to a learned profession or whose occupation requires a high level of training and proficiency.

Source: *Black's Law Dictionary*, Seventh Edition (St. Paul, MN: West Publishing, 1999).

- C. Like other professionals, appraisers must perform ethically to maintain public trust. Ethical principles are rules of conduct that are used to distinguish right from wrong.

1. The ETHICS RULE has four sections:
 - a. Conduct
 - b. Management
 - c. Confidentiality
 - d. Record Keeping
2. However, the ETHICS RULE covers three areas of an appraiser's activities:
 - a. General conduct
 - b. Development (gathering and analyzing information)
 - c. Communication (including reporting and other forms)

These ethical obligations exist for all portions of USPAP.

D. Like other professionals, appraisers must keep abreast of changes in their field to perform competently, as required in the COMPETENCY RULE and Standards Rules 1-1(a), 4-1(a), 6-1(a), 7-1(a), 9-1(a), and the Comment to STANDARD 3.

1. An individual who is not competent in appraisal practice will not have the required knowledge and experience to interpret and apply the requirements of USPAP.
2. Competent performance requires both proper judgment and proper execution.
3. The appraisal profession is continually devising new appraisal methods and techniques.
4. It is not sufficient for appraisers simply to maintain the skills and proficiency they possessed upon their entry into the profession. Appraisers should continually work to improve their skills through readings, seminars, courses, etc.

For appraising to be recognized by the public as a profession, the providers of appraisal services must develop their opinions, conclusions, and resulting reports in a manner that users believe to be credible and reliable. These activities also must not be misleading or biased. Appraisers must be ethical and competent. The PREAMBLE to USPAP sets the tone for professionalism with such statements as *the purpose of the Uniform Standards of Professional Appraisal Practice (USPAP) is to promote and maintain a high level of public trust in appraisal practice...and it is essential that appraisers develop and communicate their analyses, opinions, and conclusions to intended users of their services in a manner that is meaningful and not misleading.*

As stated previously, included in this notion of “trust” is a relationship that requires the professional to provide more than skill or expertise. There is a distinct ethical obligation to act in behalf of the public interest, not out of self-interest or in a biased manner in the interest of a client goal.

III. Valuation Services and Appraisal Practice

Some professional services that relate to asset value are properly designated as *appraisal practice*, and are subject to USPAP, while others are not.

Individuals who provide appraisals may also be involved in other professional endeavors. Therefore, it is necessary to differentiate the activities that are described as appraisal practice, and thus subject to USPAP, from activities that are not appraisal practice but still may be related to value (other valuation services).

As a result, a definition of *valuation services* is included in USPAP to indicate the broadest group of services related to any aspect of property “value.” Appraisers or non-appraisers may perform these services. In addition, USPAP includes a definition for *appraisal practice* as a particular subset of *valuation services* that has unique characteristics.

The broad concept of valuation services includes all types of services related to property value. *Valuation services* is defined in USPAP as:

services pertaining to aspects of property value.

Comment: Valuation services pertain to all aspects of property value and include services performed both by appraisers and by others.

Appraisal practice is a narrower category that is a part of the broader *valuation services*. The concept of appraisal practice carries the obligation that the valuation service is provided by an individual acting in a professional manner and as an appraiser—that is, someone who is expected to perform valuation services competently and in a manner that is independent, impartial, and objective (see definition of *appraiser*). *Appraisal practice* is defined in USPAP as:

valuation services performed by an individual acting as an appraiser, including but not limited to appraisal, appraisal review, or appraisal consulting.

Appraiser is defined as:

one who is expected to perform valuation services competently and in a manner that is independent, impartial, and objective.

Comment: Such expectation occurs when individuals, either by choice or by requirement placed upon them or upon the service they provide by law, regulation, or agreement with the client or intended users, represent that they comply. (See PREAMBLE.)

Many appraisers have other professional roles in addition to their appraiser role. For example, some appraisers are also brokers, attorneys, accountants, mortgage brokers, or consultants. These other services may include *valuation services* but are not *appraisal practice* and, therefore, do not require compliance with USPAP.

Whether or not a particular activity may be subject to USPAP is partially determined by the activity and partially determined by the role of the person who is performing the activity. If an individual is not an *appraiser*, he or she need not comply with USPAP in providing *valuation services*.

If the service falls within appraisal practice and is performed by an appraiser, it should (or must, depending on law, regulation, agreement with the client, or choice) be performed according to USPAP. If the service falls outside of appraisal practice and is performed by someone who, at least part of the time, acts as an appraiser, the appraiser must be very clear about what role he or she is performing in that task. If the individual is expected to perform that service in the role of an appraiser (as defined in USPAP), then the service should (or must) be performed according to USPAP. If the individual is not expected to perform that service in the role of an appraiser (as defined in USPAP), then the service need not be performed according to USPAP. It is the responsibility of the appraiser not to be misleading regarding the role he or she is performing when providing a *valuation service* outside of *appraisal practice*.

For example, a property manager (not an appraiser) may be asked to provide an owner with a survey of area market rents (not an opinion of appropriate market rent for the owner's building) and would not need to comply with USPAP because he/she is not an appraiser. On the other hand, an appraiser who is asked to perform this service as an appraiser should perform the service in compliance with USPAP. Furthermore, the service must be performed under USPAP when required by law, regulation, or agreement with the intended users. If, however, it is not required (by law, regulation, or agreement with the intended users) that the service be performed according to USPAP, and if the person makes it clear that he or she is not performing the service as an appraiser, then the service may be performed in a manner that is not in compliance with USPAP.

Not all valuation services comply with the ethical principles required by USPAP. If a particular valuation service has compensation arrangements that are contrary to the ETHICS RULE, a person who is an appraiser should not do the work if it falls within appraisal practice. If the service is not part of appraisal practice, then the individual who is an appraiser (but also provides other professional services) can do the work but cannot represent 1) that he or she is performing the service as an appraiser, or 2) that the service is in compliance with USPAP. If an individual who is an appraiser agrees to provide a valuation service that is not appraisal practice and in which he/she cannot truthfully sign the appraiser's certification, the appraiser must communicate with his or her client to ensure that the client and any other intended user of that service are not misled as to the role the individual is playing in performing the valuation service.

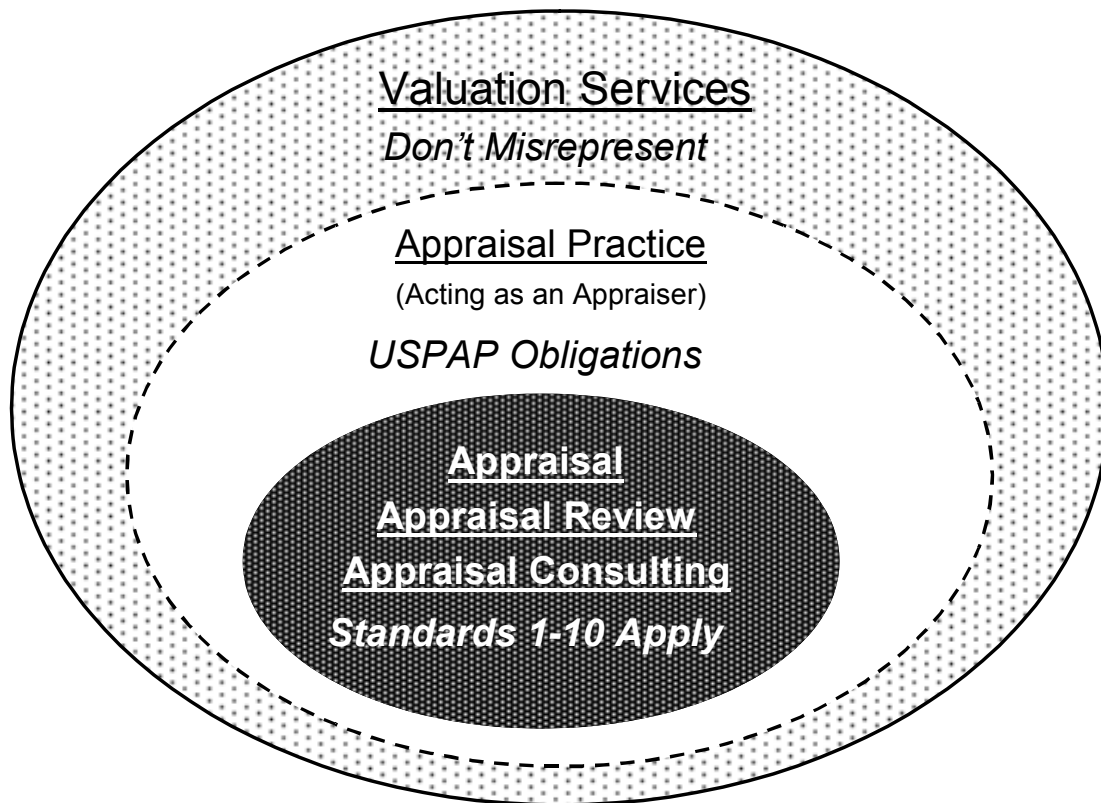
Again, a valuation service provided by an individual "as an appraiser" falls within appraisal practice. Some valuation services performed by an individual as an appraiser have Standards Rules that apply to them and some do not. Those for which there are no specific Standards Rules would need to be performed in compliance with the PREAMBLE and the applicable Rules.

If a person's identity as an appraiser, appraisal expertise, and ethical reputation with respect to appraiser independence contribute to his or her being chosen to provide a service, and the service involves value, the service is part of appraisal practice and should be performed in compliance with USPAP. This concept is underscored in the Comment to the definition of *appraisal practice*:

Appraisal practice is provided only by appraisers, while valuation services are provided by a variety of professionals and others. The terms appraisal, appraisal review, and appraisal consulting are intentionally generic and are not mutually exclusive. For example, an opinion of value may be required as part of an appraisal review and is required as a component of the analysis in an appraisal consulting assignment. The use of other nomenclature for an appraisal, appraisal review, or appraisal consulting assignment (e.g., analysis, counseling, evaluation, study, submission, or valuation) does not exempt an appraiser from adherence to the Uniform Standards of Professional Appraisal Practice.

In summary, USPAP clarifies the differences between *valuation services*, which are performed by many professionals, including appraisers, and *appraisal practice*, which pertains solely to those valuation services performed only by appraisers and requiring independence, impartiality, and objectivity. This distinction rests on whether the practitioner is functioning in the role of an *appraiser*.

The following graphic, from AO-21, illustrates the scope and coverage of USPAP in appraisal practice; and the table illustrates how the distinctive characteristics of a valuation service can be used to determine whether the service is part of appraisal practice and, if so, whether there are any Standards Rules that apply to the service.



Valuation Services (large light-shaded oval): When providing valuation services, the obligation for an individual recognized in some circumstances as an appraiser is not to misrepresent his or her role.

Appraisal Practice (dotted-line oval): Within valuation services is appraisal practice (i.e., valuation services provided by an individual acting as an appraiser). All services performed as part of appraisal practice must comply with USPAP. The portions of USPAP that apply generally to appraisal practice include the DEFINITIONS, PREAMBLE, the Conduct, Management, and Confidentiality sections of the ETHICS RULE, the COMPETENCY RULE, the JURISDICTIONAL EXCEPTION RULE and the SUPPLEMENTAL STANDARDS RULE.

Appraisal, Appraisal Review, Appraisal Consulting (dark-shaded oval within Appraisal Practice oval): Within appraisal practice, there are requirements that apply to developing and communicating appraisal, appraisal review, or appraisal consulting assignments in addition to those that apply to all appraisal practice. These requirements are described by STANDARDS 1 – 10 and the Record Keeping section of the ETHICS RULE.

VALUATION SERVICES			
	Other Roles (e.g. brokerage, property management)	Appraisal Practice	
		Other Services	Appraisal, Appraisal Review & Appraisal Consulting
Pertains to aspects of value	√	√	√
Performed by individual acting as an appraiser		√	√
Obligation to comply with USPAP		√	√
Performance and reporting requirements (STANDARDS 1-10)			√
Record keeping and workfile requirements			√

IV. Structure of USPAP

- A. The *Uniform Standards of Professional Appraisal Practice* include the DEFINITIONS section, PREAMBLE, Rules (including the ETHICS RULE, COMPETENCY RULE, DEPARTURE RULE, JURISDICTIONAL EXCEPTION RULE, and SUPPLEMENTAL STANDARDS RULE), STANDARDS 1 through 10, and Statement Nos. 1 through 10.

In USPAP, the Standards Rules include the appraisal of real property, personal property, intangible property including business interests, and mass appraisal of a defined universe of real or personal properties; appraisal review; and real property appraisal consulting (STANDARDS 1 through 10). In those appraisal practice assignments for which there are no Standards Rules, appraisers are required to comply with the DEFINITIONS, the PREAMBLE, the Conduct, Management, and Confidentiality sections of the ETHICS RULE, and the COMPETENCY, JURISDICTIONAL EXCEPTION, and SUPPLEMENTAL STANDARDS RULES. Such services could include teaching appraisal courses, providing sales data, and writing educational texts.

Comments, which are extensions of the DEFINITIONS, Rules, and Standards Rules, provide interpretation and establish the context and conditions for application. They are an integral part of USPAP and have the same weight as the component they address.

Other guidance material is bound with USPAP; this consists of 25 active Advisory Opinions—which are another form of communication published by the Appraisal Standards Board—and an Index. Such guidance material is included in the same publication for convenience of reference only. Reference to the Advisory Opinions in USPAP or in this course does not incorporate that guidance

into the Rules, Standards, or Statements that make up USPAP. In other words, these other communications do not carry the same weight and authority as the Uniform Standards themselves. It is important to differentiate between USPAP itself and other elements that are bound in the document with it.

With two exceptions, the 10 STANDARDS are paired. STANDARD 1 addresses the development of an appraisal involving real property value opinions and the use of recognized methods and techniques, while STANDARD 2 deals with the reporting of a real property appraisal in a manner that is not misleading. Similarly, STANDARDS 4 and 5 are concerned with developing and reporting real property appraisal consulting services, STANDARDS 7 and 8 with developing and reporting personal property appraisals, and STANDARDS 9 and 10 with developing and reporting business appraisals. STANDARDS 3 and 6 are not paired. STANDARD 3 is concerned with appraisal review and reporting, and STANDARD 6 deals with mass appraisal and reporting.

A clear distinction must be made between the activities involved in developing opinions and conclusions (covered in the Standards Rules addressing development) and the reporting of those opinions and conclusions.

1. STANDARD 1 addresses the procedure to be followed in developing a real property appraisal.
2. STANDARD 2 addresses the reporting of a real property appraisal and provides three options for report formats.
3. STANDARD 3 addresses the procedure for reviewing the work of another appraiser in an assignment and reporting the results of that review; an assignment under STANDARD 3 can include or exclude the reviewer's own opinion of value.
4. STANDARD 4 addresses the development of a real property appraisal consulting service. *Appraisal consulting* applies only to assignments performed by an appraiser, when the assignment result requires, as a component of developing the recommendations or conclusions, using or developing an opinion of real property value. Here again, an assignment completed in accordance with STANDARD 4 is one without advocacy.
5. STANDARD 5 addresses the reporting of a real property appraisal consulting service.
6. STANDARD 6 addresses the development and reporting of mass appraisals.
7. STANDARD 7 addresses the development of a personal property appraisal.
8. STANDARD 8 addresses the reporting of a personal property appraisal.
9. STANDARD 9 addresses the development of a business or intangible asset appraisal.

10. STANDARD 10 addresses the reporting of a business or intangible asset appraisal.

B. The structure of USPAP related to the Appraisal Process

The overall structure of USPAP is described in the PREAMBLE.

The objectives that are set by any professional standards of practice define the character of the service by establishing expectations that are reasonable for those who rely on the service. Such objectives help to distinguish good practice from bad practice based on what does, or does not, conform to the objectives.

The primary objective of USPAP is to promote and maintain a high level of public trust in professional appraisal practice. From this objective all other objectives in USPAP follow. The Rules establish intermediate objectives, which are necessary to accomplishing the primary objective. In addition to the Rules, the objectives set forth in the Standards Rules specify certain actions within specific appraisal disciplines relating to appraisal, appraisal review, and appraisal consulting.

To understand USPAP, it is important to see how its various parts complement the primary goal of promoting and preserving public trust. The PREAMBLE describes how these parts fit together and sets forth the following general principle:

It is essential that appraisers develop and communicate their analyses, opinions, and conclusions to intended users of their services in a manner that is meaningful and not misleading.

In this context the terms *meaningful* and *not misleading* have distinct ethical implications. The PREAMBLE clearly sees the appraiser as providing a service that requires *integrity, impartiality, objectivity, independent judgment, and ethical conduct*. These attributes of the service constitute essential aspects of the appraiser's opinion, which cause it to be trustworthy and reliable. For example, opinions that are biased or not impartial derive their meaning from the interests they favor. Such opinions lack substance and objectivity because they are not rooted in an acceptable process or derived in an independent manner.

While ethical principles provide an important context for a service, they do not provide solutions to problems. The term *meaningful* implies that the appraiser's solution is relevant to the client's problem and adequate for the intended users. Appraisers clearly need to provide competent service, as required in the PREAMBLE.

USPAP manages both the ethical side and the performance side of appraisal practice through a series of Rules and requirements. The Rules in USPAP cover general practice policies and the requirements elaborate on these policies for specific disciplines and assignment types. The requirements are contained in Standards and are labeled as either binding requirements or specific requirements.

Analyze the specific wording of each Standards Rule. Four words are of particular importance: *and*, *or*, *should*, and *must*. If parts of the Rule are connected by *or*, only one of these parts needs to be shown in the facts of the example; if the parts are connected by *and*, all parts need to be shown. The word *should* indicates that the actions described are desirable and ethical, but not required. The word *must*, however, indicates actions that are mandatory under the general Rules or Standards Rules.

There is a distinct method by which competent appraisers apply their knowledge and skills to the solution of valuation problems. The method is called the appraisal process, and it is one of the sources of standards for professional appraisal practice. The process is common to the different appraisal disciplines and is what unifies the disciplines into a single profession.

The appraisal process is described as a systematic procedure employed to provide an answer to a client's question about value.² The process provides a model for resolving all kinds of valuation problems, regardless of whether the subject matter is real property, personal property, or a business. Though the most common type of appraisal assignment involves an opinion of market value or fair market value (in business appraisal), the model provides the framework for developing any type of value opinion.

The organization of requirements set forth in the Standards Rules in USPAP complements the appraisal process. Each Standards Rule sets forth the requirement for competency in the area of practice addressed by the Standard. This requirement appears in Standards Rules 1-1, 4-1, 6-1, 7-1, and 9-1, and in the Comment to STANDARD 3. This competency requirement includes three elements:

- Correctly employ recognized methods and techniques
- Exercise reasonable due diligence in the collection and analysis of data and information
- Exercise a reasonable standard of care to avoid significant errors

The appraisal process may be divided into five action steps. However, as can be seen, there are sub-steps within some of these. The specific number of action steps could be described in a different manner; this is just used as a tool to demonstrate the flow of the process. Each must be completed competently. The action steps are:

1. Define the problem to be solved.

This step requires an appraiser to identify the essential elements of the problem. Correctly completing this action step allows the appraiser to

2. *The Appraisal of Real Estate*, 12th ed. (Chicago: Appraisal Institute, 2001), 49.

make a reasonable determination of the appropriate scope of work to employ in the assignment. Elements to be identified:

- Client and other intended user(s)—see definitions of *client* and *intended user* in USPAP
- Intended use of the appraiser’s opinions and conclusions—see definition of *intended use* in USPAP
- Type and Definition of Value
- Effective date(s) of the appraiser’s opinions and conclusions
- The subject property and the relevant characteristics of the subject property
- Assignment conditions, including any supplemental standards, jurisdictional exceptions, limiting conditions, extraordinary assumptions, or hypothetical conditions

2. Determine the scope of work.

Scope of Work [as defined in USPAP]—*the amount and type of information researched and the analysis applied in an assignment. Scope of work includes, but is not limited to, the following:*

- *the degree to which the property is inspected or identified;*
- *the extent of research into physical or economic factors that could affect the property;*
- *the extent of data research; and*
- *the type and extent of analysis applied to arrive at opinions or conclusions.*

The scope of work is acceptable when it is consistent with:

- The expectations of participants in the market for the same or similar appraisal services
- What the appraiser’s peers’ actions would be in performing the same or a similar assignment in compliance with USPAP

Therefore, the scope of work decision is primarily dependent upon the intended users and intended use of the assignment results. Depending on the scope of work, the DEPARTURE RULE may be invoked.

Elements in the scope of work decision:

- Intended use
- Intended users
- Type and Definition of value
- Effective date(s)
- Relevant property characteristics
- Assignment conditions

Appraiser's Burden of Proof

An appraiser must have sound reasons in support of the scope of work decision and must be prepared to support the decision to exclude any information or procedure that would appear to be relevant to the client, an intended user, or the appraiser's peers in the same or a similar assignment.

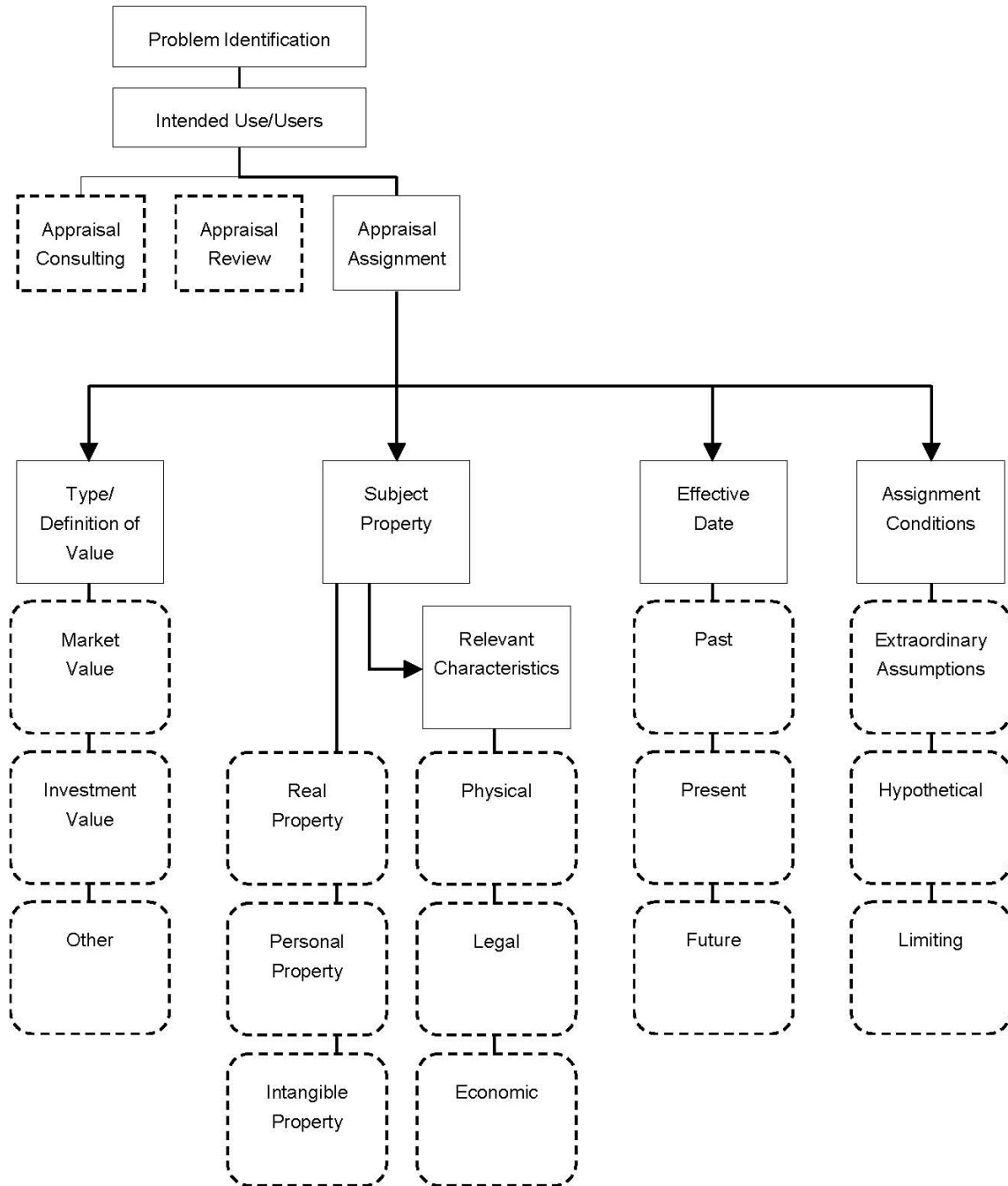
An appraiser must not allow assignment conditions or other factors to limit the extent of research or analysis to such a degree that the resulting opinions and conclusions developed in an assignment are not credible in the context of the intended use of the appraisal.

USPAP, Comment to Standards Rule 1-2 (f)

A word that is used frequently throughout USPAP is *credible*. Although no definition is included in the USPAP document, *Webster's Dictionary* defines credible as "offering reasonable grounds for being believed." Webster distinguishes the *credible* from the *plausible* by pointing out that the latter only appears to be true but may be false though not deliberately so, while the former is believed to be true because it is supported by evidence and logic.

The diagram on the following page incorporates all the assignment identifications that are required for determining the appraisal problem to be solved and that then flow into the appraiser's scope of work decision.

Scope of Work



3. Collect, verify, and analyze all relevant information.

The data and information collected must be those items necessary to solve the problem in the assignment. Statement No. 7 provides information in the context of a real property or a personal property appraisal assignment that all appraisers can use to help make appropriate scope of work decisions. The methods and techniques employed to develop problem-solution indicators in the analysis of data and information must be, at a minimum, sufficient to develop credible opinions and conclusions.

4. Reconcile the quality and quantity of the information analyzed.

An appraiser must take into account the quality and quantity of the data and information available and the applicability and suitability of the analyses completed. The objective of the reconciliation process is to reach final opinions and conclusions that are credible.

5. Report the assignment results.

The manner in which the appraiser's opinions and conclusions are communicated can range from a terse oral presentation to a highly detailed written document. The *Uniform Standards of Professional Appraisal Practice* do not prescribe the form or format of written reports, but do set forth content requirements for various types (options) of written reports.

- C. USPAP includes Statements on Appraisal Standards (SMTs). A Statement is described as follows:

Statements on Appraisal Standards are authorized by the by-laws of The Appraisal Foundation and are specifically for the purposes of clarification, interpretation, explanation, or elaboration of the Uniform Standards of Professional Appraisal Practice (USPAP). Statements have the full weight of a Standards Rule and can be adopted by the Appraisal Standards Board (ASB) only after exposure and comment.

The Appraisal Standards Board of The Appraisal Foundation has issued 10 Statements, seven of which are currently active. SMTs 6 and 7 were revised effective January 1, 2005.

Statements on Appraisal Standards

SMT-1	<i>Appraisal Review—Clarification of <u>Comment</u> on Standards Rule 3-1(g): Retired</i>
SMT-2	<i>Discounted Cash Flow Analysis</i>
SMT-3	<i>Retrospective Value Opinions</i>
SMT-4	<i>Prospective Value Opinions</i>
SMT-5	<i><u>Confidentiality</u> Section of the ETHICS RULE: Retired</i>
SMT-6	<i>Reasonable Exposure Time in Real Property and Personal Property Market Value Opinions</i>
SMT-7	<i>Permitted Departure from Specific Requirements in Real Property and Personal Property Appraisal Assignments</i>
SMT-8	<i>Electronic Transmission of Reports: Retired</i>
SMT-9	<i>Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions</i>
SMT-10	<i>Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction</i>

- D. In addition to Statements on Appraisal Standards, the ASB issues Advisory Opinions (AOs). These are approved and published by the Appraisal Standards Board as guidance. For convenience, Advisory Opinions and other reference materials are bound with USPAP. However, they are not a part of the *Uniform Standards of Professional Appraisal Practice*. To clarify the intent and purpose of such guidance material, the following text appears at the beginning of every Advisory Opinion:

This communication by the Appraisal Standards Board (ASB) does not establish new standards or interpret existing standards. Advisory Opinions are issued to illustrate the applicability of appraisal standards in specific situations and to offer advice from the ASB for the resolution of appraisal issues and problems.

The ASB has published 27 Advisory Opinions (AOs), 25 of which are currently active. AO-6 was retired effective January 1, 2005.

Advisory Opinions

- AO-1 *Sales History*
- AO-2 *Inspection of Subject Property Real Estate*
- AO-3 *Update of a Prior Assignment*
- AO-4 *Standards Rule 1-5(b)*
- AO-5 *Assistance in the Preparation of an Appraisal*
- AO-6 *The Appraisal Review Function: Retired*
- AO-7 *Marketing Time Opinions*
- AO-8 *Market Value vs. Fair Value in Real Property Appraisals*
- AO-9 *The Appraisal of Real Property That May Be Impacted by Environmental Contamination*
- AO-10 *The Appraiser-Client Relationship: Retired*
- AO-11 *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*
- AO-12 *Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2*
- AO-13 *Performing Evaluations of Real Property Collateral to Conform with USPAP*
- AO-14 *Appraisals for Subsidized Housing*
- AO-15 *Using the DEPARTURE RULE in Developing a Limited Appraisal*
- AO-16 *Fair Housing Laws and Appraisal Report Content*
- AO-17 *Appraisals of Real Property with Proposed Improvements*
- AO-18 *Use of an Automated Valuation Model (AVM)*
- AO-19 *Unacceptable Assignment Conditions in Real Property Appraisal Assignments*
- AO-20 *An Appraisal Review Assignment That Includes the Reviewer's Own Opinion of Value*

- AO-21 *USPAP Compliance*
- AO-22 *Scope of Work in Market Value Appraisal Assignments, Real Property*
- AO-23 *Identifying the Relevant Characteristics of the Subject Property of a Real Property Appraisal Assignment*
- AO-24 *Normal Course of Business*
- AO-25 *Clarification of the Client in a Federally Related Transaction*
- AO-26 *Readdressing (Transferring) a Report to Another Party*
- AO-27 *Appraising the Same Property for a New Client*

END OF  SECTION

SECTION B

***Uniform Standards of Professional Appraisal Practice:* DEFINITIONS and Rules**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with how terms set forth in USPAP are defined and used in the document. See I; *Uniform Standards of Professional Appraisal Practice*, DEFINITIONS.
- Recognize the significance of the Comments to the Standards. See II; *Uniform Standards of Professional Appraisal Practice*, PREAMBLE.
- Demonstrate familiarity with the topics described in the ETHICS RULE. See III, A; *Uniform Standards of Professional Appraisal Practice*, ETHICS RULE.
- Recognize when the Record Keeping section of the ETHICS RULE applies in an assignment. See III, A, 4; *Uniform Standards of Professional Appraisal Practice*, ETHICS RULE.
- Identify the competency requirement that must be met before accepting an assignment. See III, B; *Uniform Standards of Professional Appraisal Practice*, COMPETENCY RULE.
- Identify the elements necessary to correctly determine the scope of work that is appropriate and necessary in an assignment, and the circumstances under which an appraiser may depart from certain specific requirements. See III, C; *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE.
- Recognize the applicability of the JURISDICTIONAL EXCEPTION RULE. See III, D; *Uniform Standards of Professional Appraisal Practice*, JURISDICTIONAL EXCEPTION RULE.
- Realize that government agencies, government sponsored enterprises, and other entities that establish public policy may require supplemental standards, and recognize the types of requirements that are, and are not, addressed in the SUPPLEMENTAL STANDARDS RULE. See III, E; *Uniform Standards of Professional Appraisal Practice*, SUPPLEMENTAL STANDARDS RULE.
- Analyze examples to determine if a specific behavior violates any Rule of USPAP and, if so, suggest how a violation might have been avoided. See Discussion Examples: Rules.

Uniform Standards of Professional Appraisal Practice: DEFINITIONS and Rules

The Appraisal Standards Board periodically issues Statements and Advisory Opinions. The following Statements and Advisory Opinions should be studied in conjunction with this section:

- SMT-7: *Permitted Departure from Specific Requirements in Real Property and Personal Property Appraisal Assignments*
- SMT-9: *Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions*
- SMT-10: *Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction*

Guidance:

- AO-9: *The Appraisal of Real Property That May Be Impacted by Environmental Contamination*
- AO-13: *Performing Evaluations of Real Property Collateral to Conform with USPAP*
- AO-14: *Appraisals for Subsidized Housing*
- AO-15: *Using the DEPARTURE RULE in Developing a Limited Appraisal*
- AO-25: *Clarification of the Client in a Federally Related Transaction*
- AO-27: *Appraising the Same Property for a New Client*

I. Terms from the DEFINITIONS Section of USPAP

The DEFINITIONS section identifies how specific terms or phrases are used in USPAP. The first line of text in the DEFINITIONS section states, *For the purpose of the Uniform Standards of Professional Appraisal Practice (USPAP), the following definitions apply.* Note that a term defined in USPAP may have a different or additional meaning in another context.

A. Review the various definitions.

As guidance, compare how the term *market value* is defined for use in the context of USPAP with an example of a definition of market value that **might** be used in an assignment. The “definition” in USPAP is actually a description of the parts of a definition of market value and is not, in itself, a definition. The appraiser must take care to identify the correct definition of value used in an assignment and avoid presuming that all definitions of market value are the same. The same is true of the definition of *fair market value*, the term more commonly

used in business valuation. Note that the source of the value definition used in a real property appraisal must be cited in a Self-Contained or Summary Appraisal Report [Standards Rule 2-2(a) and (b)]. Comparable requirements exist for personal property and business appraisal reports.

II. PREAMBLE

- A. Purpose of USPAP
 - 1. To establish requirements for professional appraisal practice
 - 2. To promote and maintain a high level of public trust in professional appraisal practice
- B. For whose benefit is the *Uniform Standards of Professional Appraisal Practice* prepared?
 - 1. Providers of appraisal services
 - 2. Users of appraisal services
- C. What appraisal services are covered by USPAP?
 - 1. Appraisal
 - 2. Appraisal review
 - 3. Real property appraisal consulting

NOTE: Refer also to AO-21, *USPAP Compliance*.

- D. What property types are covered by USPAP?
 - 1. Tangible (real and personal property)
 - 2. Intangible (business interests and others)
- E. Comments within Rules and Standards Rules

What are Comments to USPAP?

Comments are an integral part and extension of USPAP and have the same weight as the component they address. These extensions of the DEFINITIONS, Rules, and Standards Rules provide interpretation and establish the context and conditions for application.

III. The Rules

A. ETHICS RULE

- Promote and preserve public trust
- Requirement for an appraiser to maintain a high level of public trust in appraisal practice

These establish the purpose of USPAP and address the issue of jurisdiction. Implementation and enforcement of USPAP occurs through its adoption, citation, or reference by an agency or other public body, or an organization, client, or client group with the ability to establish requirements for either the service the appraiser performs or the appraiser. The requirement to comply with USPAP may also occur as a result of an agreement to comply between the appraiser and the client, or by the appraiser's choice.

- Test for applicability of USPAP
- An appraiser's obligation not to misrepresent his or her role when providing valuation services that are outside appraisal practice

This places the burden on the appraiser to be clear in disclosure to a client and other intended users about what the service does and does not include.

- Sections—Conduct, Management, Confidentiality, and Record Keeping
- Activities covered—general conduct, development, communication

These establish the fundamental obligations of an appraiser as part of the profession.

NOTE: Refer to SMT-9, *Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions*. As guidance, see AO-25, *Clarification of the Client in a Federally Related Transaction*, and AO-27, *Appraising the Same Property for a New Client*.

1. Conduct—The Appraiser Must/Must Not

Note that this section addresses not only the Conduct portion of the ETHICS RULE, but also all portions of USPAP that would be categorized as ethical conduct requirements.

Related to General Conduct:

- a. Must perform ethically and competently, in accordance with USPAP and any supplemental standards agreed to by the appraiser in accepting the assignment.
- b. Must not engage in criminal conduct.

Related to Development:

- c. Must perform with impartiality, objectivity, and independence. Differentiation of these terms is provided below, as taken from *Webster's Dictionary*.

Impartial = mental state that does not favor one side over another at the outset of an investigation

Objective = opposed to subjective, based on what exists and what is known rather than on preconceived or personal views

Independent = freedom from outside influences or controls

- d. Must not perform as an advocate for any party or issue.
- e. Must not accept assignments with predetermined opinions and conclusions.
- f. Must not use or rely on **unsupported** conclusions relating to race, color, religion, national origin, gender, marital status, familial status, age, receipt of public assistance income, handicap, or unsupported conclusions that homogeneity of such characteristics is necessary to maximize value.

Related to Communication (of which Reporting is a part):

- g. Must not communicate assignment results in a misleading or fraudulent manner.
- h. Must not use or communicate a misleading or fraudulent report.
- i. Must not permit an employee or other person to communicate a misleading or fraudulent report.

2. Management

- a. Must disclose any fees, commissions, or things of value paid in the procurement of an assignment.

- b. Must not accept an assignment, or have a compensation arrangement for an assignment, that is contingent on any of the following:
 - i. The reporting of a predetermined result,
 - ii. A direction in assignment results that favors the cause of the client,
 - iii. The amount of a value opinion,
 - iv. The attainment of a stipulated result, or
 - v. The occurrence of a subsequent event directly related to the appraiser's opinions and specific to the assignment's purpose.
- c. Must not advertise for or solicit assignments in a manner that is false, misleading, or exaggerated.

3. Confidentiality

- a. The confidential nature of the appraiser-client relationship must be protected.
- b. To whom may an appraiser disclose confidential information?³
 - i. Client and those authorized by the client,
 - ii. State enforcement agencies and such third parties as authorized by law, and
 - iii. Duly authorized professional peer review committees (if authorized by law).

NOTE: As guidance, refer to AO-27, *Appraising the Same Property for a New Client*, on related issues.

4. Record Keeping

- a. An appraiser must prepare a workfile for each appraisal, appraisal review, or appraisal consulting assignment that includes:

3. Appraisers should take particular note of applicable laws or regulations, such as federal legislation and regulations, regarding personal, non-public information in the handling of information obtained or used in an assignment.

- i. The name of client and identity, by name or type, of other intended users,
 - ii. True copies of any written reports documented on any type of media (note that a *true copy* includes the signed pages therein, such as the certification and any letter of transmittal, etc., that would include a signature),
 - iii. Summaries of oral reports or testimony, or a transcript of testimony including a signed and dated certification, and
 - iv. All other data, information, and documentation necessary to support the appraiser's opinions and conclusions and show compliance with the Record Keeping section and all other applicable Standards.
- b. Workfile retention
- i. At least five (5) years after preparation, or two (2) years after final disposition of any judicial proceeding in which the appraiser provided testimony related to the assignment, whichever period expires last.
 - ii. An appraiser must have custody of his or her workfile or make appropriate workfile retention, access, and retrieval arrangements with the party that does have custody of the workfile.

B. COMPETENCY RULE

The COMPETENCY RULE requires appraisers to have the knowledge and experience to complete an assignment competently and contains requirements for appraisers who are not sufficiently competent at the beginning of an engagement.

Competency is reflected in correct judgment and correct execution.

Judgment is involved in correctly identifying the problem to be solved and the appropriate scope of work necessary to solve the problem, as well as in many other instances during the appraisal process.

Correct execution takes place during the development and reporting of an appraisal. According to USPAP, the appraiser must:

- 1. Identify the problem to be solved, and
- 2. Have the knowledge and experience to complete the assignment competently, or
- 3. Disclose the lack of knowledge/experience to the client in advance, and
 - a. Take all steps to complete the assignment competently, and

- b. Describe the lack of knowledge/experience and steps taken in the report.

NOTE: As guidance, see AO-9, *The Appraisal of Real Property That May Be Impacted by Environmental Contamination*, AO-13, *Performing Evaluations of Real Property Collateral to Conform with USPAP*, and AO-14, *Appraisals for Subsidized Housing*.

C. DEPARTURE RULE

The DEPARTURE RULE applies when appraisers exempt themselves from specific requirements according to their scope of work decision. Such a scope of work reduction may occur when adherence to certain requirements is **not necessary** for the development of **credible assignment results**, but when the requirement may generally be thought to be **applicable**. This scope of work decision is subject to client approval and entails certain disclosure obligations (under the DEPARTURE RULE) so that intended users of the report understand the limitations on the assignment results.

It is important to understand that the concept of departure is not a starting point of a decision within USPAP, but is simply a result of the scope of work decision. Scope of work is a broader concept than departure, for departure only relates to disclosure regarding specific requirements. The term is defined in USPAP as follows:

***Scope of Work:** the amount and type of information researched and the analysis applied in an assignment. Scope of work includes, but is not limited to, the following:*

- *the degree to which the property is inspected or identified;*
- *the extent of research into physical or economic factors that could affect the property;*
- *the extent of data research; and*
- *the type and extent of analysis applied to arrive at opinions or conclusions.*

The DEPARTURE RULE is the narrowest and least controlling of the Rules in USPAP. The ETHICS, COMPETENCY, JURISDICTIONAL EXCEPTION, and SUPPLEMENTAL STANDARDS RULES control many aspects of an assignment, not just specific requirements.

1. Permits exception from strict observance of specific requirements of USPAP provided that:
 - a. The scope of work will result in credible opinions and conclusions, and

- b. The appraiser makes appropriate disclosure in the report.
2. Standards Rules that are identified as binding requirements are always required unless the JURISDICTIONAL EXCEPTION RULE applies.
3. Standards Rules that are identified as specific requirements may be departed from provided that prior to entering into such an agreement:
 - a. The appraiser determines that the appraisal process is not so limited that results are not credible, and
 - b. The client is advised that the assignment is less than or different from the specific requirements and the report will clearly identify and explain the departure(s), and
 - c. The client agrees to the limited appraisal service as appropriate for the intended use.
4. Not all specific requirements are applicable to every assignment. If the specific requirement is truly not applicable, then it is irrelevant, and no departure is needed.

Example

In real property appraisals, three approaches to value generally apply—cost, income, and sales comparison. If the property appraised is not an income type of property, such as a residence in an owner-occupied market, the income approach is typically not applicable. Therefore, no departure is required if only the cost and sales comparison approaches are used. However, the elimination of the income approach must be explained.

5. A specific requirement is applicable when it addresses:
 - a. Factors or conditions present in the assignment, or
 - b. Analysis that is typical practice in such assignment.
6. A specific requirement is not applicable when it addresses:
 - a. Factors or conditions not present in the assignment, or
 - b. Analysis not typical practice in such an assignment, or
 - c. Analysis that would not provide meaningful results.
7. If the specific requirement is necessary to produce credible results, then departure is not permitted.
8. Departure is permitted when a specific requirement is applicable, but not necessary to produce credible results.

9. A specific requirement is both applicable and necessary when it addresses:
 - a. Factors or conditions present in the assignment, or
 - b. Analysis that is typical practice, and
 - c. Lack of consideration would significantly affect the credibility of the results.
10. Typical practice for a given assignment is measured by:
 - a. Expectations of participants in the marketplace for appraisal services, and
 - b. What an appraiser's peers would typically do in the same or a similar assignment.
11. If an appraiser departs from a specific requirement that would otherwise be required by USPAP, the departure must be disclosed in any report, written or oral.
12. When departure is invoked, the appraisal is called a Limited Appraisal. Although USPAP reporting Standards require that the report of a Limited Appraisal state and explain any permitted departures from specific requirements of the development Standards, and the reason for excluding any of the usual appraisal approaches, USPAP does not require that the appraisal be specifically identified as a Limited Appraisal. However, some state laws may require such identification.
13. Departure is not permitted from Standards Rules 1-1, 1-2, 1-5, 1-6, 2-1, 2-2, 2-3, 3-1, 3-2, 3-3, 4-1, 4-2, 5-1, 5-2, 5-3, 6-1, 6-3, 6-6, 6-7, 6-8, 7-1, 7-2, 7-5, 7-6, 8-1, 8-2, 8-3, 9-1, 9-2, 9-3, 9-5, 10-1, 10-2, and 10-3.
14. Departure does not apply to the DEFINITIONS, PREAMBLE, ETHICS RULE, COMPETENCY RULE, JURISDICTIONAL EXCEPTION RULE, or SUPPLEMENTAL STANDARDS RULE.

NOTE: Refer to SMT-7, *Permitted Departure from Specific Requirements in Real Property and Personal Property Appraisal Assignments*, and, as guidance, to AO-15, *Using the DEPARTURE RULE in Developing a Limited Appraisal*.

D. JURISDICTIONAL EXCEPTION RULE

The JURISDICTIONAL EXCEPTION RULE recognizes that other laws or regulations may take precedence over USPAP regulations in certain situations. Because it is not the intent of USPAP to have authority over the existing laws and regulations of the various state and federal jurisdictions, when a part of USPAP is contrary to law or public policy of any jurisdiction, that part is of no force. Jurisdictional exception is defined in USPAP as *an assignment condition that voids the force of a part or parts of USPAP, when compliance with part or*

*parts of USPAP is contrary to law or public policy applicable to the assignment.*⁴ Application of the JURISDICTIONAL EXCEPTION RULE is a matter of applicable law, regulation, etc. It is not a matter of choice by the appraiser.

1. If any part of USPAP is contrary to law or public policy, only that part is void and has no force or effect in that jurisdiction.
2. For proper use of the JURISDICTIONAL EXCEPTION RULE, it is necessary to understand that:
 - a. When jurisdictional exception applies, it must be disclosed.
 - b. *Law* means a body of rules with binding legal force established by a controlling government authority, such as federal and state constitutions, legislative and court-made law, and administrative rules, regulations, and ordinances.
 - c. *Public policy* refers to well-defined moral and ethical standards recognized by the courts with the aid of statutes, judicial precedents, and other similar evidence.
 - d. *Jurisdiction* relates to the legal authority at the federal, state, and local levels of government.
3. Note that the application of a jurisdictional exception is not a choice between the appraiser and the client; rather it is a condition of a particular assignment due to applicable law or public policy. The use of this exception is based on a conflict that originates from law or public policy and thus the appraiser is required to cite the legal authority that justifies the exception to USPAP.

E. SUPPLEMENTAL STANDARDS RULE

The SUPPLEMENTAL STANDARDS RULE enables government agencies, government sponsored enterprises, and other entities that establish public policy to establish additional development or reporting requirements. Such additional requirements are recognized by USPAP so long as they do not detract from or diminish the purpose of USPAP and are material to the development or reporting of assignment results.⁵

4. The proper exercise of the JURISDICTIONAL EXCEPTION RULE requires disclosure of the legal authority justifying the appraiser's disregard for a part or parts of USPAP. A legal authority is one that has the power to legislate, apply, or interpret law. Attorneys or other professionals who advise people in the law do not constitute "legal authority" as this phrase is used in the JURISDICTIONAL EXCEPTION RULE.

5. The 2002 version of USPAP changed the sources of supplemental standards to include only government agencies, government sponsored enterprises, and entities that establish public policy. Previous editions of USPAP included financial institutions, asset managers, large client groups, etc. These organizations can still utilize their additional appraisal requirements in their engagement and qualification processes, but they are no longer considered to be supplemental standards as defined in USPAP. Examples of requirements from a government agency that have a material effect on the development and reporting processes are included in the Interagency Appraisal and

continued on next page

Supplemental standards are published in regulations, rules, policies, and other similar documents. In order to be a supplemental standard under USPAP, a requirement must have the same applicability to all properties or assignments in a particular category or class regardless of the contracting entity. Supplemental standards are different from other contractual agreements that are unique to the contracting entity and apply specifically to a particular property or assignment. When an appraiser accepts an assignment that includes acceptable supplemental standards, he or she is obligated to competently satisfy those supplemental standards, as well as applicable USPAP requirements.

NOTE: Refer to SMT-10, *Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction*, and as guidance, to AO-25, *Clarification of the Client in a Federally Related Transaction*.

Discussion Examples: DEFINITIONS and Rules

- A. Most of the residential loans in Nickelville and the surrounding area are made by Central Bank; the rest are made by two small commercial banks. The only state certified residential appraiser in town does all of Central's appraisals in and around Nickelville, and this is a substantial part of her work. There are several licensed real estate brokers who render market value opinions as a secondary business.

Recently, new management has taken over Central, and the institution has become much more aggressive in making loans. Loan officers now operate on a commission basis and actively seek new loans.

In recent weeks several appraisals have come in below the proposed sale prices. Each time this happens, the loan officer calls the appraiser in to "discuss" the appraisal. The loan officers and the selling brokers are pressuring her to "go along" with the deal. In one case, there was only a few hundred dollars difference on a \$90,000 value, but in several others the proposed sale prices were at the extreme top end of the value ranges indicated by the comparables. In one case, the proposed price was outside the range entirely. The appraiser tries to use the best, most recent comparables and feels that she does careful, objective appraisals. She sincerely wants to be of service to her clients and is concerned; in this case, she is not doing so. What latitude within USPAP does the appraiser have?

Evaluation Guidelines, October 27, 1994 of the federal regulatory agencies (OCC, OTS, FDIC, FRB). These guidelines require that appraisals include the current market value of the property in its actual physical condition and subject to the zoning in effect as of the date of the appraisal (a current date of value). This requirement has a material effect on the type of opinion developed. Likewise, the requirement that appraisals include sufficient information and analysis to support the institution's decision to engage in the transaction has a material effect on the amount of information to provide in an appraisal report. Examples of requirements that do not have a material effect on development or reporting and, therefore, would not qualify as supplemental standards include software preferences, file formats, report forms, report exhibits, etc.

- B. A certified general appraiser prepared an appraisal report of a motel in May 1997, and testified about the appraisal in court in June 1998. The trial court issued its decision in July 1998. The decision was appealed, and in December 1998, the appellate court remanded the case to the trial court for further consideration. The trial court considered the case in July 2000, and that decision was appealed. The appeal is still pending. How long should the appraiser keep his workfile?
- C. A fee appraiser is trying to get on the approved list for a local mortgage company. To be considered for approval, the lender requires an appraiser to provide “sample” appraisal reports performed within the past year. The lender also requires each appraiser to pay a fee to be included on the lender’s approved appraiser list. Is there a way the appraiser can provide the sample appraisal reports under USPAP? Also, is it ethical for the appraiser to pay a fee to the lender?
- D. An appraiser has been asked by Global Relocation Corporation to appraise the home of a transferring employee. The owners are at home when the appraiser arrives to inspect the house. They follow him around, pointing out features of the house as he makes his inspection. As the appraiser prepares to leave, the owner asks, “Well, what’s it worth?” The appraiser patiently explains the appraisal process, pointing out that this is only the first step and much work needs to be done before he will have an opinion of the house’s value. The next day he is finishing the appraisal when the telephone rings. It’s the owner and he wants to know the value opinion. The appraiser tells him the value conclusion and is careful to fulfill the requirements for an oral report as stated in **STANDARD 2** of the *Uniform Standards of Professional Appraisal Practice*. Has the appraiser conducted himself properly?
- E. Two months ago an appraiser appraised a property for a lender. The sale, which was pending at the time of the appraisal, ultimately fell through and the loan was never made. The appraiser has just been asked by another lender to appraise the property for financing in connection with a new purchase agreement. The appraiser is wondering whether or not he can accept this assignment. Under what conditions **might** he accept this assignment? Is it acceptable for him simply to change the client’s name on the report?
- F. An appraiser was recently asked to update an appraisal performed by another appraiser who works for a different appraisal company. Can the appraiser prepare an update if another appraiser performed the original appraisal?
- G. A certified residential real property appraiser’s business has been slow lately and she occasionally has the opportunity to perform commercial appraisals with a certified general real property appraiser. To date, she has only been involved with the preparation of a few small commercial properties. However, the appraiser recently received a call from a client for a fee quote on a full-service car wash. Since she has prepared appraisals on other commercial properties, she believes she can adequately prepare an appraisal on a car wash facility. May she take the assignment? Does her being a certified residential appraiser affect her taking the assignment?

- H. The property owner's attorney in a condemnation case has asked a real property appraiser to invoke the **JURISDICTIONAL EXCEPTION RULE** of USPAP in a particular commercial property case. **Standards Rule 1-5** requires appraisers to analyze any prior sales of the property being appraised that occurred within three years. The subject property sold within one year of the appraisal for what everyone admits was a very low price, although all parties claim the sale was not made under duress. For this reason, the attorney does not want the prior sale mentioned in the appraisal report; however, the appraiser reviews USPAP with the attorney, showing him **Standards Rule 1-5** (which prohibits departure) and the definition of *binding requirements* in USPAP. The attorney is aware that the **JURISDICTIONAL EXCEPTION RULE** exists and tells the appraiser to invoke it for this situation. How should the appraiser respond?
- I. A client recently asked a certified residential appraiser to reduce his fee for appraisals in instances where the loans do not close. The client indicated he would be willing to pay extra for other assignments in return. Would this practice be ethical?
- J. A personal property appraiser has prepared an appraisal of the personal property in an estate and plans to charge a fee based upon the aggregate value of the estate properties appraised. Does USPAP permit the appraiser to structure his fee in this way?
- K. A client asked an appraiser to eliminate a cost approach in an appraisal assignment of a newer house, but not to prepare a Limited Appraisal. The appraiser concludes that the cost approach, although applicable, is not necessary to produce credible conclusions. He is unsure, since he considered the approach, whether the assignment is a Complete or Limited Appraisal. He is also uncertain whether he should include a cost approach in his workfile although he is not performing the approach to value in his appraisal. Is the assignment considered a Complete Appraisal or a Limited Appraisal? Is he required to include the omitted approach in his workfile?
- L. An appraiser just received an assignment that involves a city lot that is improved with two residences. The client has requested that he appraise the site and only the main residence, without mentioning the other structure. The appraiser is unsure how to proceed and wonders if it is ethical to accept this assignment. Does USPAP permit him to accept the assignment as requested?
- M. A certified general appraiser recently developed and orally reported a Complete Appraisal of a hotel's real property as part of a tax appeal. The opposing attorney, under discovery, requests the appraiser's workfile, which will include his signed certification. The appraiser is amused, as he put nothing in writing specifically to avoid having to show it to the opposing side. Is he in compliance with USPAP?

- N. An attorney client has requested a “Limited-Summary Appraisal” from a certified general appraiser. The appraiser wants to comply and he completes the assignment based on what he understands these terms to mean, using only minimum research. He is careful to write “Limited-Summary Appraisal” on the title page because he is sure this is a USPAP requirement. Is this correct? What are the USPAP requirements concerning types of appraisals and reports?

END OF



SECTION

SECTION C

Uniform Standards of Professional Appraisal Practice: **STANDARD 1—** **Real Property Appraisal, Development**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 1 and its Standards Rules. See I–VI; *Uniform Standards of Professional Appraisal Practice*, STANDARD 1, Standards Rules 1-1, 1-2, 1-3, 1-4, 1-5, and 1-6, including the Comments.
- Recognize that departure is not permitted from Standards Rules 1-1, 1-2, 1-5, and 1-6. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 1-1, 1-2, 1-5, and 1-6.
- Analyze examples to determine if a specific behavior violates the Standards Rules relating to STANDARD 1 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARD 1.

Uniform Standards of Professional Appraisal Practice: **STANDARD 1—** **Real Property Appraisal, Development**

The basic requirements for developing a real property appraisal are presented in STANDARD 1, which states: *In developing a real property appraisal, an appraiser must identify the problem to be solved and the scope of work necessary to solve the problem, and correctly complete research and analysis necessary to produce a credible appraisal.* Six Standards Rules follow this statement.

The Standards Rules can be divided into two categories: binding requirements and specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in developing a properly supported value opinion. For example, whenever a specific requirement is necessary to the development of credible results, the appraiser must comply with the requirement. Invoking the DEPARTURE RULE is only necessary if a specific requirement is “applicable” to the assignment. (See the DEPARTURE RULE.) The binding requirements under STANDARD 1 are Standards Rules 1-1, 1-2, 1-5, and 1-6. Standards Rules 1-3 and 1-4 are specific requirements. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

The requirements of STANDARD 1, which apply to real property appraisal, are very similar to those of STANDARDS 4, 7, and 9, which apply to appraisal consulting services, personal property appraisal, and business appraisal, as well as to those in the Standards Rules found in the first parts of STANDARDS 3 and 6, which apply to appraisal review and mass appraisal. While other specialized areas of appraisal practice covered under these Standards involve different types of property or practice, the basic rules for developing an opinion of value or a conclusion are generally similar to those in STANDARD 1.

At the end of STANDARD 1, use the Discussion Examples provided to explore the applications of the Standards Rules.

The definitions of the following terms should be reviewed in relation to STANDARD 1:

Appraisal

Complete Appraisal

Limited Appraisal

Market Value

The Appraisal Standards Board periodically issues Statements and Advisory Opinions. The following Statements and Advisory Opinions should be studied in conjunction with STANDARD 1:

- SMT-2: *Discounted Cash Flow Analysis*
- SMT-3: *Retrospective Value Opinions*
- SMT-4: *Prospective Value Opinions*
- SMT-9: *Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions*
- SMT-10: *Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction*

Guidance:

- AO-1: *Sales History*, in conjunction with Standards Rule 1-5(a) and (b)
- AO-2: *Inspection of Subject Property Real Estate*
- AO-3: *Update of a Prior Assignment*, in conjunction with STANDARD 1
- AO-4: *Standards Rule 1-5(b)*, in conjunction with Standards Rule 1-5(b)
- AO-7: *Marketing Time Opinions*, in conjunction with Standards Rule 1-2
- AO-8: *Market Value vs. Fair Value in Real Property Appraisals*
- AO-17: *Appraisals of Real Property with Proposed Improvements*, in conjunction with Standards Rule 1-4(h)
- AO-18: *Use of an Automated Valuation Model (AVM)*
- AO-19: *Unacceptable Assignment Conditions in Real Property Appraisal Assignments*
- AO-22: *Scope of Work in Market Value Appraisal Assignments, Real Property*
- AO-23: *Identifying the Relevant Characteristics of the Subject Property of a Real Property Appraisal Assignment*
- AO-24: *Normal Course of Business*
- AO-25: *Clarification of the Client in a Federally Related Transaction*
- AO-27: *Appraising the Same Property for a New Client*

I. Standards Rule 1-1 (Binding)

- A. The requirement to **correctly employ** is established through two means:
 - 1. The accepted texts and course materials of college appraisal courses and nationally recognized professional appraisal organizations, and/or
 - 2. Court decisions in the jurisdiction(s) in which the appraisal, appraisal review, or appraisal consulting assignment is conducted.
- B. The admonition that *each appraiser must continuously improve his or her skills to remain proficient in real property appraisal* reinforces the mandate for continuing education contained in the COMPETENCY RULE.
- C. Further, it should be noted that USPAP prohibits two types of errors:
 - 1. Substantial errors, and
 - 2. A series of small errors that may not significantly affect the results if taken separately but that may compromise the credibility of those results when taken in the aggregate.
- D. As noted previously, USPAP is a recital of the ways in which an appraiser, whether performing an appraisal, an appraisal review, or a real property appraisal consulting assignment, is expected to exercise due diligence and due care. This point is brought out in the Comment on Standards Rule 1-1(c).
- E. All of Standards Rule 1-1 is a binding requirement, from which departure is not permitted.

II. Standards Rule 1-2 (Binding)

USPAP requires an appraiser to identify:

- A. The client and other intended users (see AO-25, *Clarification of the Client in a Federally Related Transaction*), and
- B. The intended use of the appraiser's opinions and conclusions.

NOTE: The intended use may be by a client or an intended user that is one of the entities qualified under the SUPPLEMENTAL STANDARDS RULE (i.e., government agencies, government sponsored enterprises, or other entities that establish public policy). If that entity has issued appraisal requirements that supplement the requirements in USPAP, the appraiser is required by USPAP to ascertain whether those requirements apply as supplemental standards in the assignment (see the SUPPLEMENTAL STANDARDS RULE; also see AO-25, *Clarification of the Client in a Federally Related Transaction*).

- C. The type and definition of value applicable in the assignment, and, if a market value opinion is to be developed, ascertain whether the value is to be the most probable price. (If the opinion is to be of market value, an opinion of reasonable exposure time is required. See AO-7, *Marketing Time Opinions*, as guidance. For clarification of market value vs. fair value, see AO-8, *Market Value vs. Fair Value in Real Property Appraisals*.)
- D. The effective date of the appraisal.
- E. Relevant property characteristics, including:
 - 1. Location and physical, legal, and economic attributes,
 - 2. Interest valued,
 - 3. Any personal property, trade fixtures, or intangibles included in the appraisal,
 - 4. Known easements, restrictions, encumbrances, leases, reservations, covenants, contracts, declarations, special assessments, etc., and
 - 5. Whether the subject property is a fractional interest, physical segment, or partial holding.

NOTE: If the information needed to identify these characteristics is not available, an extraordinary assumption may be necessary.

- F. Scope of work necessary to complete assignment:
 - 1. Expectations of market participants, and
 - 2. Actions of appraiser's peers in similar circumstances.

NOTE: If the assignment includes agreed-upon supplemental standards, the appraiser is obligated to address those requirements as well as the USPAP requirements in performing the assignment. For an example, refer to Part A of SMT-10, *Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction*, to ensure recognition of which parts of USPAP relate to a client group's requirements.

- G. Any extraordinary assumption, which may be used only if:
 - 1. It is required for proper development,
 - 2. The appraiser has a reasonable basis for the assumption,
 - 3. Its use produces credible results, and
 - 4. It is appropriately disclosed.

- H. Any hypothetical condition, which may be used only if:
 - 1. It is clearly required for legal purposes, reasonable analysis, or comparison,
 - 2. Its use produces credible results, and
 - 3. It is appropriately disclosed.

III. Standards Rule 1-3 (Departure Permitted)

Specific requirements for developing a real property appraisal include:

- A. Identification and analysis of factors that affect property use, and
- B. Development of a highest and best use opinion.

NOTE: An appraiser must analyze the relevant legal, physical, and economic factors to the extent necessary to support the appraiser's highest and best use conclusion(s).

IV. Standards Rule 1-4 (Departure Permitted)

This Standards Rule includes specific requirements for the application of the three traditional approaches to property appraisal, when applicable, and other components of the analysis.

- A. Sales comparison approach
- B. Cost approach
 - 1. Site valuation,
 - 2. Cost new estimate, and
 - 3. Depreciation estimate, i.e., cost new less depreciation plus the opinion of land value provides an indication of value by the cost approach.
- C. Income approach
 - 1. Estimate of gross income potential based upon comparable rental data from the market and/or the potential earnings capacity of the property,
 - 2. Estimate of expenses based upon comparable data,
 - 3. Estimate of capitalization and/or discount rates based upon comparable data, and

4. Projections based on reasonably clear and appropriate evidence. (See SMT-2, *Discounted Cash Flow Analysis*.)
- D. When developing an opinion of the value of a leased fee estate or a leasehold estate, an appraiser must analyze the effect on value, if any, of the terms and conditions of the lease(s).
- E. An appraiser must analyze the effect on value, if any, of the assemblage of the various estates or component parts of a property and refrain from valuing the whole solely by adding together the individual values of the various estates or component parts.
- F. An appraiser must analyze the effect on value, if any, of anticipated public or private improvements, located on or off the site, to the extent that market actions reflect such anticipated improvements as of the effective appraisal date.
- G. An appraiser must analyze the effect on value of any personal property, trade fixtures, or intangible items that are not real property but are included in the appraisal.
- H. When appraising proposed improvements, an appraiser must examine and have available for future examination:
 1. Plans, specifications, or other documentation sufficient to identify the scope and character of the proposed improvements,
 2. Evidence indicating the probable time of completion of the proposed improvements, and
 3. Reasonably clear and appropriate evidence supporting development costs, occupancy projections, and the anticipated competition at the time of completion.

V. Standards Rule 1-5 (Binding)

USPAP requires the appraiser to **analyze** the types of data and information enumerated in Standards Rule 1-5.

- A. Appraisers are required to analyze (if such information is available to the appraiser in the normal course of business) all agreements of sale, options, or listings of the subject property current as of the effective date of the appraisal over the specified time periods, and
- B. Sales of the subject property require analyzing for a minimum of three (3) years prior to the effective date of the appraisal for real property.
- C. Standards Rules 2-2(a)(ix), (b)(ix), and (c)(ix) contain requirements for including the results of analyzing information gathered in compliance with Standards Rules 1-5(a) and (b). Specifically, when the type and definition of value of the assignment is to develop an opinion of market value, an appraiser must:

1. Report the result of the analysis, or
2. If such information is unavailable, disclose the efforts undertaken by the appraiser to obtain the information, or
3. If such information is irrelevant, provide a statement acknowledging the existence of the information and citing its lack of relevance.
4. The Minimum Appraisal Standard of the Federal Financial Institutions Regulatory Agencies requires the appraiser to report (“in reasonable detail”) prior sales of the property being appraised. (This would be a supplemental standard.)

NOTE: A discussion of “normal course of business” is provided in AO-24.

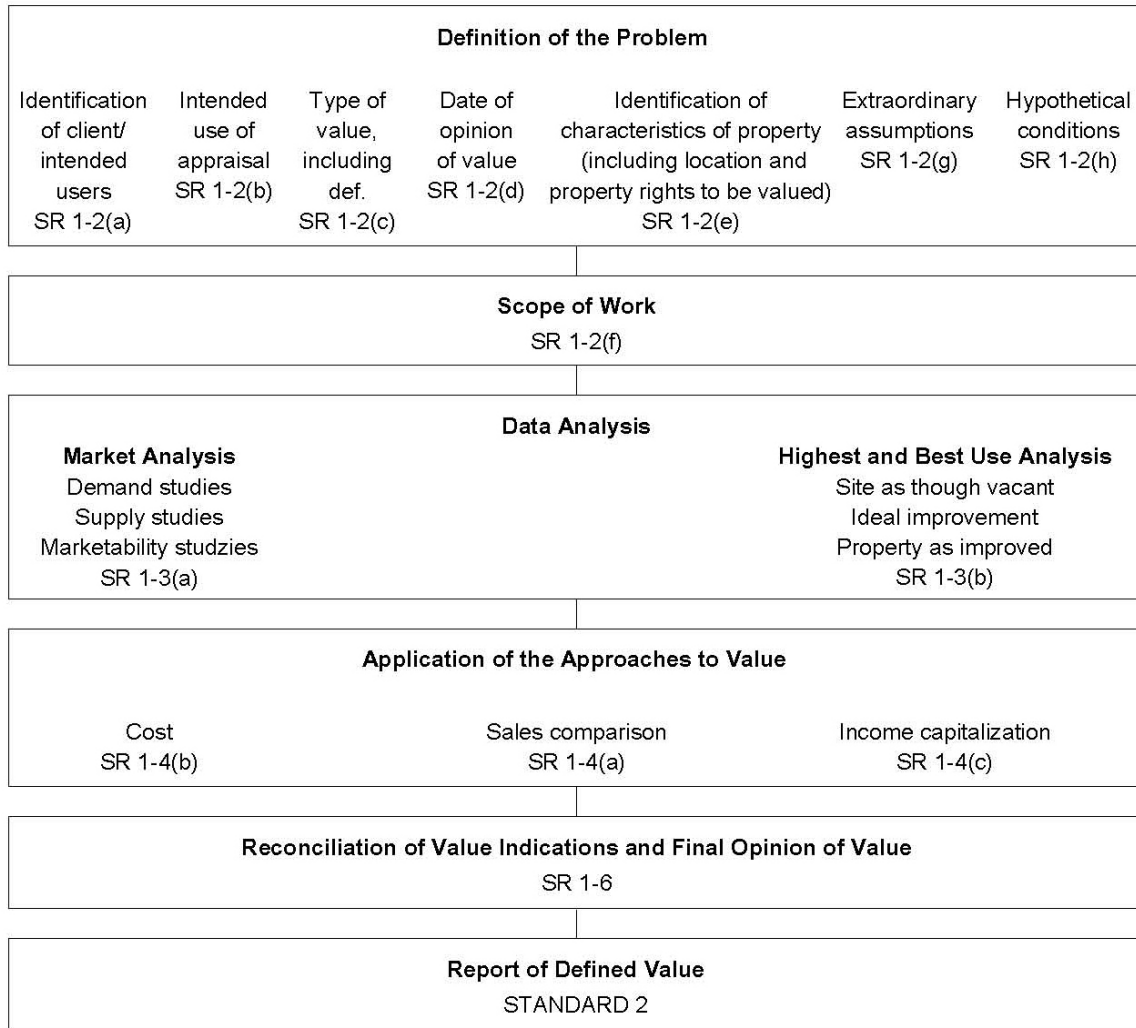
VI. Standards Rule 1-6 (Binding)

USPAP requires that the quantity and quality of data and the applicability and suitability of the approaches used be reconciled to arrive at a value conclusion.

NOTE: Regardless of what it may be called, providing a more current value or an analysis of a property that was previously appraised is simply a new assignment. (See AO-3, *Update of a Prior Assignment*.)

The following diagram incorporates the previously discussed considerations that are required for the scope of work decision, and then shows the additional requirements needed to develop credible results. This diagram follows the flow of the appraisal process addressed in Standards Rules 1-1 through 1-6.

The Appraisal Process/USPAP



Discussion Examples: STANDARD 1

- A. The vice president of 1st Savings Bank in Centertown is reviewing an appraisal of a 450-unit proposed apartment complex completed by a certified general appraiser. The value opinion is based on a very aggressive occupancy projection, yet the report contains no marketability study and only a brief statement of current vacancy rates with no support for the vacancy conclusion.

The vice president invites the appraiser to his office to discuss the appraisal. At their meeting, the appraiser points out that the client was not willing to pay for a detailed study and that he prepared the appraisal under severe time constraints. Has he made a legitimate argument?

- B. An appraiser works in the Texas office of a national appraisal firm. She was recently sent to Denver to appraise a shopping mall. She spent a day inspecting the property and interviewing the property manager, and then flew to Omaha where she was scheduled to meet with another client.

Back at her office, the appraiser made several calls to Denver appraisers requesting comparable sales and rental data, but she got little information. Instead, she used information on Texas shopping centers that she had on file to complete the appraisal report. Later she received a letter from an FDIC reviewer who was highly critical of her appraisal. He said that she failed to consider several important, relevant sales of Denver-area shopping centers indicating values substantially different from her conclusion. Do the circumstances of her schedule relieve her of the responsibility to learn the nuances of the market? Is the appraiser allowed to do an appraisal in a state in which she has no experience?

- C-1. The client is a major developer of ski resorts. He has contacted an appraiser and asked him to provide an opinion of the market value of the total assets of a resort he is considering purchasing. The client emphasizes that he is not interested in an allocation of the assets among the categories tangible real, tangible personal, and intangibles. The appraiser is confused. He is certain that USPAP requires him to allocate or separately value the non-realty items. Is he correct? Must he allocate the total assets? Is it appropriate for him to accept the assignment?

- C-2. A local hotel developer has applied for a permanent loan on his hotel. The lender has contacted a certified general appraiser and requested an appraisal. The intended use is underwriting a real estate loan. The loan officer has requested the market value of the total assets with no allocation among the components. He has told the appraiser to “just call it market value of the hotel.” Must the appraiser allocate the assets in this case?

- D. An appraiser is retained by Stillwater Bank to review values of the real property that serve as collateral for the loan portfolio of Valley Bank, a small banking association that Stillwater wants to acquire. An appraiser with many years of residential experience has done most of Valley’s appraisal work.

All the appraisals are completed on a URAR. The number of minor errors and inconsistencies the review appraiser finds in almost every report troubles her. The value opinions, however, are accurate. The appraiser seems annoyed when confronted about the quality issue. He stresses that USPAP does not require perfection. Is he correct?

- E. A residential appraiser offers the quickest turnaround and the lowest fees in town. In order to do this she has become very efficient. She completes her property inspections in 10 minutes, using the city assessor's database for the site and building dimensions, and enters data on the subject property directly into her laptop computer on the site. Her comparable sales with color photographs come directly from the MLS database and she does not inspect them. It is not unusual for her to complete 10 appraisals a day and electronically transmit them to her clients.

Recently, two of her appraisals have come under fire. In one case, her best comparable was sold under duress, a situation that would have been revealed by verification with a participant to the transaction. Another comparable is in a neighborhood that is in an entirely different price range from the subject, but this fact was not revealed in the report. In another appraisal, the size of the subject was actually 400 square feet different from that reported in the city assessor's records and affected the property value. The appraiser explained that there is no way she can measure each subject property, look at all the comparables and talk to a participant, and still meet her turnaround commitments, much less earn a respectable fee. Is she required to measure the subject improvements and inspect and verify her comparables?

- F. A real property appraiser has been asked to appraise a surplus parcel of land at market value. The date of the appraisal will be prior to its advertisement for sale by the local community public works department. According to the public works director, a covenant will be placed on the land immediately prior to the sale that will restrict its use to open space or recreation. The value opinion in the appraisal is to reflect the title condition. The property is in use by the public works department and the use limitation is not in place. Since the appraiser knows the "as is" condition of the property title is not as the director indicated, can he do the appraisal as if the covenant were in place? If so, which is involved in the assignment, an extraordinary assumption or a hypothetical condition?
- G. An appraiser has been asked to value an eight-house subdivision, which has yet to sell a single unit. All eight houses are the same model, so the appraiser prepares one URAR, then multiplies the value conclusion by eight and reports the product as his conclusion of the market value of all eight houses. He has been told that he may do the assignment this way as long as there are fewer than 10 units involved. Is this acceptable?
- H. Appraiser A has been retained to appraise a 45-acre parcel in Hopeville for a local property owner as of a retrospective date two years ago. He prepares a Self-Contained Appraisal Report that includes eight land sales; most of these properties are in far superior locations on the main commercial street in

Hopeville, and no adjustment is made for this fact. He concludes that the parcel has a market value of \$6,500,000.

Appraiser B, an appraiser for the Fifth Bank of Hopeville, is looking over Appraiser A's appraisal. Something is familiar, but she cannot quite place it. Suddenly it comes to her. She finds a clipping in her files indicating that the court approved a sale of the same 45-acre parcel for \$2,600,000 in cash. The property was on the market for 18 months, a full listing sheet was widely distributed, and the court found that the price was fair. The sale settled three months after the retrospective date of value.

When asked about it, Appraiser A explains that, although he was aware of it, USPAP does not require reporting a sale that occurs after the **effective** date of value. What are the correct reporting responsibilities applicable in this situation? Are there other potential problems with the assignment?

- I. A licensed residential appraiser is appraising a single-family residence for a lender. His conclusion is a market value of \$200,000. He dutifully notes that the property sold two years ago for the same amount, and has been listed for six months at \$199,999. So far, no takers have emerged. Comment on the appraiser's compliance with USPAP.
- J. In reading his state's newsletter regarding disciplinary actions against appraisers, an appraiser notices many such actions are related to flipping schemes. Being a newly certified appraiser, he is wondering what kinds of things appraisers should do to avoid being inadvertently entangled in such schemes. How does USPAP assist in this matter?

SECTION C (CONTINUED)

Uniform Standards of Professional Appraisal Practice: **STANDARD 2—** **Real Property Appraisal, Reporting**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 2 and its Standards Rules, including appraisal report options. See I–V; *Uniform Standards of Professional Appraisal Practice*, STANDARD 2, Standards Rules 2-1, 2-2, 2-3, and 2-4, including the Comments.
- Recognize that departure is not permitted from Standards Rules 2-1, 2-2, and 2-3. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 2-1, 2-2, and 2-3.
- Analyze examples to determine if a specific behavior violates the Standards Rules relating to STANDARD 2 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARD 2.

Uniform Standards of Professional Appraisal Practice: **STANDARD 2—** **Real Property Appraisal, Reporting**

STANDARD 2, which is concerned with the written or oral communication of a real property appraisal, states: *In reporting the results of a real property appraisal, an appraiser must communicate each analysis, opinion, and conclusion in a manner that is not misleading.*

The Standards Rules relating to STANDARD 2 are either binding requirements or specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in reporting a value opinion. (See the DEPARTURE RULE.) The binding requirements under STANDARD 2 are Standards Rules 2-1, 2-2, and 2-3. Only Standards Rule 2-4, regarding oral reports, is a specific requirement. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

Although Standards Rule 2-2 permits varying levels of detail in reports, Standards Rule 2-1 requires that each report contain sufficient information to enable the intended users to understand it properly. This requirement is binding in all cases.

Standards Rule 2-2 is also binding and includes three format options for appraisal reports: Self-Contained Appraisal Report, Summary Appraisal Report, and Restricted Use Appraisal Report. All reports must identify the option used.

Standards Rule 2-3, also a binding requirement, sets forth a model of the certification statement that is required in each real property appraisal report. The Comment to Standards Rule 2-3 requires that, in an assignment that includes only assignment results developed by the real property appraiser(s), any appraiser who signs a real property appraisal report must also sign the certification. In an assignment that includes personal property, business or intangible asset results not developed by the real property appraiser(s), any real property appraiser(s) who signs a certification accepts full responsibility for the real property elements of the certification, for the real property assignment results, and for the real property contents of the appraisal report. The signing appraiser(s) accepts full responsibility for all elements of the certification, for the assignment results, and for the contents of the report. Furthermore, when a signing appraiser(s) has relied on work done by others who do not sign the certification, the signing appraiser is responsible for the decision to rely on their work. The signing appraiser(s) is required to have a reasonable basis for believing that those individuals performing the work are competent and that their work is credible. This also applies to reviewers who sign the report. If a reviewer does not wish to be responsible for the contents of the appraisal report under review, he or she must follow the proper methodology for preparing an appraisal review report, as covered in STANDARD 3.

Standards Rule 2-4 deals with requirements for an oral report. Although departure is allowed, appraisers are again reminded to ensure that the requirements of Standards Rule 2-1 are met (i.e., clear, accurate, sufficient information, not misleading, etc.). The oral report should meet the requirements for a Summary Appraisal Report.

At the end of STANDARD 2, use the Discussion Examples provided to explore the applications of the Standards Rules.

The definitions of the following terms should be reviewed in relation to STANDARD 2:

Report

Appraisal Report

The Appraisal Standards Board periodically issues Statements and Advisory Opinions. The following Advisory Opinions should be studied in conjunction with STANDARD 2:

Guidance:

- AO-5: *Assistance in the Preparation of an Appraisal*, in conjunction with Standards Rule 2-3
- AO-11: *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*, in conjunction with Standards Rule 2-2
- AO-12: *Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2*, in conjunction with Standards Rule 2-2
- AO-16: *Fair Housing Laws and Appraisal Report Content*, in conjunction with STANDARD 2
- AO-26: *Readdressing (Transferring) a Report to Another Party*, in conjunction with STANDARD 2

I. STANDARD 2 Overview

The Comment to STANDARD 2 indicates that it governs (1) the **content** and (2) the **level of information** of any report *that communicates the results of a real property appraisal*. Note that STANDARD 2 governs the reporting of real property appraisals only. STANDARD 3 contains the reporting requirements for appraisal reviews; STANDARD 5 applies to real property appraisal consulting assignments; STANDARD 6 contains the reporting requirements for mass appraisal assignments; STANDARD 8 applies to personal property appraisals; and STANDARD 10 to business and intangible asset appraisals.

II. Standards Rule 2-1 (Binding)

This Standards Rule covers **written** and **oral** real property appraisal reports.

- A. One major ethical violation by an appraiser in reporting the results of an appraisal is to mislead readers and users of the appraisal report.
- B. Without setting specific minimum standards or specifications, Standards Rule 2-1(b) requires that an appraiser include in both written and oral reports *sufficient information to enable the intended users of the appraisal to understand the report properly*. It is not necessary to teach the reader how to do an appraisal, but is necessary to provide enough information that he/she can understand the report itself.
 - 1. The persons expected to use a Self-Contained or Summary Appraisal Report might include parties other than the client. Only the client is expected to use a Restricted Use Appraisal Report.
 - 2. Statement No. 9 (SMT-9: *Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions*) provides additional information about the appraiser's obligations to the client and to intended users.
- C. All extraordinary assumptions, hypothetical conditions, and limiting conditions used in the assignment must be reported **clearly and conspicuously**. In addition, the fact their use might have affected the assignment results must be indicated.
 - 1. *Hypothetical condition* and *extraordinary assumption* are defined terms in USPAP. Review if necessary.
 - 2. Any application of the DEPARTURE RULE, indicating a Limited Appraisal, would be an assumption or extraordinary assumption. One example would be the elimination of the income approach on instructions from counsel for the client. Another example would be the elimination of the cost approach, again on instructions from the client.

NOTE: Eliminating a research or analysis step that is a specific requirement in response to instructions of the client or a client's representative does not eliminate the appraiser's obligation (burden of proof) to support the scope of work decision.

III. Standards Rule 2-2 (Binding)

This Standards Rule deals with contents and characteristics of **written** appraisal reports. It provides for three options:

- A. Self-Contained Appraisal Report,
- B. Summary Appraisal Report, and

- C. Restricted Use Appraisal Report.
- D. All written appraisal reports must prominently state which option is used. (See AO-11, *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*, and AO-12, *Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2*.) The Record Keeping section of the ETHICS RULE also provides information about the relationship between written reports and workfiles.
1. Both the client and the other intended users must be identified.
 2. The intended use of the appraisal must also be identified.
 3. Both the real estate and the real property interest being appraised must be identified. One means for describing the real estate is a legal description. However, USPAP does not require a legal description.
 4. When developing an opinion of market value, the definition cited should be consistent with the requirements of the jurisdiction in which the property is located (when the appraisal is conducted in anticipation of legal proceedings), the requirements of the client (to the extent that they are not inconsistent with standard professional appraisal practice as represented by USPAP), or such influences on value definitions as required by the Federal Financial Institutions Regulatory Agencies.
 5. Note that both the effective date of the appraisal (appraisal date, as of date) and the date of the appraisal report must be included in the appraisal report. The date of the report is usually the date of any transmittal letter.
 6. Standards Rules 2-2(a)(vii), 2-2(b)(vii), and 2-2(c)(vii) address what is referred to as the scope of the appraisal, or the part of the appraisal report that describes in summary fashion the data obtained, from where and how, and how the data were applied to standard appraisal procedures or approaches. The following disclosure was added in the 2001 edition of USPAP:

When any portion of the work involves significant real property appraisal assistance, the appraiser must describe the extent of that assistance. The signing appraiser must also state the name(s) of those providing the significant real property appraisal assistance in the certification, in accordance with SR 2-3.
 7. Standards Rules 2-2(a)(viii), 2-2(b)(viii), and 2-2(c)(viii) identify that an appraiser must clearly and conspicuously disclose the use of all extraordinary assumptions, hypothetical conditions, and limiting conditions; and state that their use might have affected the assignment results.

8. Depending on the type of report, Self-Contained (Standards Rule 2-2 (a)), Summary (Standards Rule 2-2 (b)), or Restricted Use (Standards Rule 2-2 (c)), Section (ix) varies substantially. In a Self-Contained Appraisal Report, the appraiser must **describe** the information analyzed, the procedures followed, and the reasoning that supports the analyses, opinions, and conclusions. In a Summary Appraisal Report, these must be **summarized**, and in a Restricted Use Appraisal Report, they must only be **stated**. However, for a Restricted Use Appraisal Report, a specific, coherent workfile must be prepared sufficient for the appraiser to produce a Summary Appraisal Report.
9. If the assignment does not involve developing an opinion of market value, the appraiser is not required to develop a highest and best use opinion.
10. Under Standards Rules 2-2(a)(xi), 2-2(b)(xi), and 2-2(c)(xi), the exclusion of any of the *usual valuation approaches* must be explained and supported. Remember, an approach may have been excluded because it is not applicable (which is not considered departure) or it may have been excluded because of the scope of work decision, even though the approach would normally be considered applicable (which is departure). No approach can be excluded if it is necessary for a credible result. These Standards Rules also include the catchall requirement that the written appraisal report (or other written communication, or the written workfile) contain sufficient information *to indicate that the appraiser complied with the requirements of STANDARD 1*.
 - a. Any **permitted departures** that were made because the item in the specific requirement was not applicable must be identified and explained.
 - b. Any **permitted departures** that were made because of a scope of work decision but for which the item in the specific requirement would normally be considered applicable (but not necessary for credible results) must also be clearly identified and explained, and other elements tied to the DEPARTURE RULE are necessary.
 - c. Any **unallowable departures** are exactly that: not permitted. This would apply to items in specific requirements that are necessary for credible results; they cannot be departed from. Of course, this also applies to binding requirements.
 - d. Information **required** under Standards Rule 1-5 might necessitate particular mention and discussion, if any departure from the market norm(s) is identified.

IV. Standards Rule 2-3 (Binding)

Meeting the requirements of Standards Rule 2-3 for certification indicates compliance with USPAP. A signed certification must be included in any written report. In the case of an oral report, a signed certification must be included in the workfile. A signed certification evidences an appraiser's recognition of his or her ethical obligations.

The certification requires only the disclosure of the names of those providing significant real property appraisal assistance. The nature of this assistance and any other form of significant assistance or assumptions based on reports by engineers, geologists, etc., needs to be disclosed somewhere in the report, perhaps as part of the scope of work description.

Each of the obligations included in the Comment to this Standards Rule needs to be understood. The Comment contains the following requirements:

A signed certification is an integral part of the appraisal report. An appraiser who signs any part of the appraisal report, including a letter of transmittal, must also sign this certification.

In an assignment that includes only assignment results developed by the real property appraiser(s), any appraiser(s) who signs a certification accepts full responsibility for all elements of the certification, for the assignment results, and for the contents of the appraisal report. In an assignment that includes personal, business or intangible asset assignment results not developed by the real property appraiser(s), any real property appraiser(s) who signs a certification accepts full responsibility for the real property elements of the certification, for the real property assignment results, and for the real property contents of the appraisal report.

When a signing appraiser(s) has relied on work done by others who do not sign the certification, the signing appraiser is responsible for the decision to rely on their work. The signing appraiser(s) is required to have a reasonable basis for believing that those individuals performing the work are competent and that their work is credible.

The names of individuals providing significant real property appraisal assistance who do not sign a certification must be stated in the certification. It is not required that the description of their assistance be contained in the certification, but disclosure of their assistance is required in accordance with SR 2-2(a), (b), or (c)(vii), as applicable.

- A. State licensing/certification agencies sometimes have additional, expanded certification requirements. These typically include an identification of the license or certification status (and number) of the appraiser(s) signing the appraisal report. Certain government agencies, government sponsored enterprises, or other entities that establish public policy also have additional, expanded certification requirements. (These are supplemental standards under USPAP.)

- B. Professional appraisal organizations typically have additional, expanded certification requirements. These commonly include a statement of compliance with the code of ethics and standards of professional practice of the organization in question. They may also include identification of continuing education or recertification status of the appraiser(s) signing the appraisal report. (This is not a supplemental standard under USPAP.)
- C. Individual clients may also have additional, expanded certification requirements. (This is not a supplemental standard under USPAP.)
- D. All additional certification requirements are permissible under USPAP, as long as they are not in conflict with the contents of USPAP (including the jurisdictional exception).

V. Standards Rule 2-4 (Departure Permitted)

This Standards Rule and the Comment emphasize the Record Keeping section of the ETHICS RULE for oral reports.

- A. It is not acceptable to honor a request from the client or the client's representative (such as "Don't put it in writing") if the request would cause elimination of something that is necessary to meet the requirements of Standards Rule 2-1. Substantive matters set forth in Standards Rule 2-2(b) must be addressed in each oral report.
- B. Copies of transcripts of depositions and/or testimony by the appraiser should be sought. If they are obtained, they must be kept in the appraisal file in accordance with the Record Keeping section requirements of the ETHICS RULE.

On the following page is a summary of the report options, adapted from Standards Rule 2-2 and AO-11, *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*.

Standards Rule 2-2 Report Comparison Chart

The essential difference among the three options is in the use and application of the terms “describe,” “summarize,” and “state.” “Describe” is used to connote a comprehensive level of detail in the presentation of information. “Summarize” is used to connote a more concise presentation of information. “State” is used to connote the minimal presentation of information.

a) Self-Contained Appraisal Report	b) Summary Appraisal Report	c) Restricted Use Appraisal Report
i. state the identity of the client and any intended users, by name or type;	i. state the identity of the client and any intended users, by name or type;	i. state the identity of the client, by name or type;
ii. state the intended use of the appraisal;	ii. state the intended use of the appraisal;	ii. state the intended use of the appraisal;
iii. describe information sufficient to identify the real estate involved in the appraisal, including the physical and economic property characteristics relevant to the assignment;	iii. summarize information sufficient to identify the real estate involved in the appraisal, including the physical and economic property characteristics relevant to the assignment;	iii. state information sufficient to identify the real estate involved in the appraisal;
iv. state the real property interest appraised;	iv. state the real property interest appraised;	iv. state the real property interest appraised;
v. state the type and definition of value and cite the source of the definition;	v. state the type and definition of value and cite the source of the definition;	v. state the type of value, and cite the source of its definition;
vi. state the effective date of the appraisal and the date of the report;	vi. state the effective date of the appraisal and the date of the report;	vi. state the effective date of the appraisal and the date of the report;
vii. describe sufficient information to disclose to the client and any other intended users of the appraisal the scope of work used to develop the appraisal;	vii. summarize sufficient information to disclose to the client and any intended users of the appraisal the scope of work used to develop the appraisal;	vii. state the extent of the process of collecting, confirming, and reporting data or refer to an assignment agreement retained in the appraiser’s workfile that describes the scope of work to be performed;
viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;	viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;	viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;
ix. describe the information analyzed, the appraisal procedures followed, and the reasoning that supports the analyses, opinions, and conclusions;	ix. summarize the information analyzed, the appraisal procedures followed, and the reasoning that supports the analyses, opinions, and conclusions;	ix. state the appraisal procedures followed, state the value opinion(s) and conclusion(s) reached, and reference the workfile;
x. state the use of the real estate existing as of the date of value and the use of the real estate reflected in the appraisal; and, when reporting an opinion of market value, describe the support and rationale for the appraiser’s opinion of the highest and best use of the real estate;	x. state the use of the real estate existing as of the date of value and the use of the real estate reflected in the appraisal; and, when reporting an opinion of market value, summarize the support and rationale for the appraiser’s opinion of the highest and best use of the real estate;	x. state the use of the real estate existing as of the date of value and the use of the real estate reflected in the appraisal; and, when reporting an opinion of market value, state the appraiser’s opinion of the highest and best use of the real estate;
xi. state and explain any permitted departures from specific requirements of STANDARD 1 and the reason for excluding any of the usual valuation approaches; and	xi. state and explain any permitted departures from specific requirements of STANDARD 1 and the reason for excluding any of the usual valuation approaches; and	xi. state and explain any permitted departures from applicable specific requirements of STANDARD 1; state the exclusion of any of the usual valuation approaches; and state a prominent use restriction that limits use of the report to the client and warns that the appraiser’s opinions and conclusions set forth in the report cannot be understood properly without additional information in the appraiser’s workfile; and
xii. include a signed certification in accordance with Standards Rule 2-3.	xii. include a signed certification in accordance with Standards Rule 2-3.	xii. include a signed certification in accordance with Standards Rule 2-3.

Comments have not been included in this chart.

Discussion Examples: STANDARD 2

A. An appraiser is requested to perform a Complete Appraisal and submit a Self-Contained Appraisal Report. The letter of transmittal and other sections of the document identify the report as such. In the appraisal report, the appraiser briefly *summarizes* the highest and best use section. However, the approaches to value are extremely detailed and meet the requirements of a Self-Contained Appraisal Report. Has she satisfied the requirements for a Self-Contained Appraisal Report?

B. Client X is responsible for ordering and reviewing appraisals prepared for a Thai company that is investing in properties in the United States. He retained a certified general appraiser in the United States to value a shopping center that his company was about to purchase. He explained in a letter the importance of having a detailed report since he would be in Thailand when he reviewed the appraisal. The two never had an opportunity to talk, however.

When he received the appraisal report, the comparable data were summarized with a brief statement of the appraiser's conclusions. Client X is very unhappy. What part of USPAP is intended to avoid this type of miscommunication?

C. A mortgage broker hired an appraiser to prepare an appraisal on a single-family property. He asked that she discuss her value opinion with him orally prior to transmitting the report. The appraiser completed her analysis and telephoned the client with her conclusions. The broker client was indignant and objected strongly to the value conclusion, indicating that the "figure" would not help his client's objectives. He further indicated that there would be no need to provide a written report. What are the appraiser's obligations under USPAP?

D. A bank hires a certified residential appraiser to provide residential appraisals and requires that he sign all reports completed for the client by his company.

The bank recently underwent a regulatory examination and was cited for poor quality appraisals. The senior loan officer called the appraiser and complained. The appraiser was quick to point out that he signs on the right side of the URAR under the signature block entitled, "Supervisory Appraiser" and checks the "did not inspect property" box. He explains that he cannot be held responsible for errors made by his staff appraisers, most of whom are trainees. Is he correct?

E. A new residential appraiser recently ordered appraisal form software and isn't sure what to do, as the current software available does not address the most recent USPAP changes. What should she do?

F. An appraiser has five appraisers whom he supervises and he spends long hours inspecting properties as a result. He often is away from the office when it is time to transmit an appraisal report to a client, so his assistant signs his reports. Does this create any USPAP issues?

- G. An appraiser has been asked by a client to prepare a Restricted Use Appraisal Report and the client has identified in communication with the appraiser that other intended users will also receive the report. Does USPAP allow the use of this report option in such a circumstance?



SECTION D

Uniform Standards of Professional Appraisal Practice: **STANDARD 3—** **Appraisal Review, Development and Reporting**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 3 and its Standards Rules. See I–III; *Uniform Standards of Professional Appraisal Practice*, STANDARD 3, Standards Rules 3-1, 3-2, 3-3, and 3-4, including the Comments.
- Recognize that departure is not permitted from Standards Rules 3-1, 3-2, and 3-3. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 3-1, 3-2, and 3-3.
- Recognize when statements in an appraisal review report indicate that the appraiser performing the review did or did not develop his or her own opinion of value. As Guidance, see Advisory Opinion (AO) 20, *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*.
- Analyze examples to determine if a specific behavior violates the Standards Rules relating to STANDARD 3 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARD 3.

Uniform Standards of Professional Appraisal Practice: STANDARD 3— Appraisal Review, Development and Reporting

The basic requirements for the development and reporting of an appraisal review assignment are presented in STANDARD 3, which states: *In performing an appraisal review assignment, an appraiser acting as a reviewer must develop and report a credible opinion as to the quality of another appraiser's work that was performed as part of an appraisal, appraisal review, or appraisal consulting assignment and must clearly disclose the scope of work performed.*

The Standards Rules related to STANDARD 3 can be divided into two categories: binding requirements and specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in developing or reporting a properly supported review opinion. For example, whenever a specific requirement is necessary to the development of credible results, the appraiser must comply with the requirement. An appraiser can depart from a specific requirement only when the requirement can be classified as “applicable” to the assignment. Invoking the DEPARTURE RULE is only necessary if a specific requirement is “applicable” to the assignment. (See the DEPARTURE RULE.) Standards Rules 3-1, 3-2, and 3-3 are binding. Standards Rule 3-4 (regarding oral review reports) is a specific requirement. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

At the end of STANDARD 3, use the Discussion Examples provided to explore the applications of the Standards Rules.

The definition of the following term should be reviewed in relation to STANDARD 3:

Appraisal Review

The Appraisal Standards Board periodically issues Advisory Opinions for guidance on specific appraisal issues or problems. The following Advisory Opinion should be studied in this section.

Guidance:

- AO-20: *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*

I. Independent, Third-Party Appraisal Review

- A. See the DEFINITIONS section for the specific definition of *appraisal review* in this context.

- B. An appraiser performing an appraisal review assignment is referred to in USPAP simply as a *reviewer*. (As guidance, refer to AO-20, *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*, for additional discussion of terminology.)
- C. An appraiser performing an appraisal review may review all or any part of a completed work or a service performed by another appraiser. Therefore, a clear understanding and description of the scope of work is essential.
- D. Note very carefully the distinction between a supervisor or an employer cosigning an appraisal report under the conditional label of “reviewer” or “appraisal reviewer” (covered in STANDARD 2) and an independent, third-party review of the work of another appraiser (covered in STANDARD 3).
- E. An opinion of the character, quality, and supportability of a written report is part of what constitutes appraisal review work under STANDARD 3.
- F. A reviewer who develops an opinion of value for the property in the appraisal report under review (or conclusion, in a review involving a consulting assignment) must comply with all the applicable Standards Rules of STANDARD 1 for real property, STANDARD 4 for real property appraisal consulting, STANDARD 6 for mass property, STANDARD 7 for personal property, or STANDARD 9 for intangible property. The reviewer’s report of this opinion is governed by STANDARD 3, not STANDARD 2, 6, 8, or 10. (As guidance, refer to AO-20, *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*.)
- G. The Comment to STANDARD 3 specifically notes that *a reviewer performing an appraisal review must not sign the work under review unless he or she intends to accept the responsibility of a cosigner of that work*. This is an important point.
- H. ***A misleading or fraudulent appraisal review report violates the ETHICS RULE.*** (Bold added for emphasis)
- I. The Comment to STANDARD 3 emphasizes that the COMPETENCY RULE also applies to reviewers.

II. Standards Rule 3-1 (Binding)

- A. Standards Rules 3-1(a) through (g) state the actions an appraiser must complete when performing an appraisal review.
- B. Standards Rule 3-1(a) requires the reviewer to identify:
 - 1. The reviewer’s client and other intended users,
 - 2. The intended use of the reviewer’s opinions and conclusions, and

3. The purpose of the assignment, i.e., is the reviewer required to develop his or her own opinion of value?
- C. Standards Rule 3-1(b) requires the reviewer to identify the:
1. Subject of the appraisal review assignment,
NOTE: The subject of a review assignment might be part of, rather than all of, another appraiser's work, such as the highest and best use analysis within an appraisal report, and might extend beyond a report to include material in a workfile.
 2. Effective date of the review,
 3. Property and ownership interest appraised in the work under review,
 4. Date of the work under review and the effective date of the conclusion in the work under review, and
 5. Appraiser(s) who completed the work under review (unless the identity was withheld).
- D. Standards Rule 3-1(c) requires the reviewer to identify the scope of the work to be performed. It also includes certain scope of work requirements under which an appraisal review must be conducted, and certain specifications that must be met if the reviewer develops his or her own opinion of value.
- E. Standards Rules 3-1 (d) through (g) require the reviewer to develop an opinion as to the:
1. Completeness of the material within the scope of work,
 2. Apparent adequacy and relevance of the data and the propriety of the adjustments to the data,
 3. Appropriateness of the appraisal methods and techniques used (within the scope of work) and reasons for any disagreement, and
 4. Appropriateness and reasonableness of analyses, opinions, and conclusions in the work under review (given the scope of work) and reasons for any disagreement.

NOTE: Recognize that the review opinions and conclusions are in the context of the scope of work applicable in the review.

III. Standards Rule 3-2 (Binding)

An appraisal review report according to Standards Rule 3-2 must incorporate all of the items addressed in Standards Rule 3-1. This is true whether the reviewer agrees with the analyses, opinions, and conclusions in the work under review or disagrees with some or all of them.

The reviewer may include his or her own opinion of value within the appraisal review report itself without preparing a separate appraisal report. However, the portion of the review report that supports the reviewer's value opinion must match, at a minimum, the reporting requirements of a Summary Appraisal Report.

- A. No personal inspection of the subject property of the work under review is required of the reviewer. It is required, however, that the reviewer report whether he or she personally inspected the subject property. Whether or not an inspection is required is part of the reviewer's scope of work decision.
- B. No independent verification of data or information contained in the appraisal documents under review is required of the reviewer unless it is required by the scope of the assignment.
- C. The required certification in Standards Rule 3-3 may be added to or expanded by clients or professional appraisal organizations, provided that the resulting expanded certification is not in conflict with the requirements and specifications of USPAP.

IV. Cross-References

- A. STANDARD 3 generally is interrelated with:
 - 1. The definition of *appraisal review* in the current edition of USPAP,
 - 2. STANDARD 1,
 - 3. Standards Rule 2-3,
 - 4. STANDARD 4,
 - 5. STANDARD 7,
 - 6. Standards Rule 8-3,
 - 7. STANDARD 9,
 - 8. Standards Rule 10-3, and
 - 9. The ETHICS RULE.
- B. Standards Rule 3-2 is directly interrelated with Standards Rule 3-1.

- C. Supplemental standards and/or jurisdictional exceptions may apply.
- D. AO-20 provides guidance for appraisers on how the reviewer's scope of work changes when the purpose of an appraisal review assignment requires the reviewer to develop and report his or her own opinion of value or consulting conclusion, and provides examples of language in appraisal review reports to indicate when the reviewer did or did not develop his or her own opinion.

V. **Applicability of the DEPARTURE RULE**

All sections of STANDARD 3 are binding requirements except Standards Rule 3-4 regarding oral reports. Therefore, the DEPARTURE RULE may not be applied to Standards Rules 3-1, 3-2, and 3-3; however, the Comment to STANDARD 3 states: *Appraisal review is the act or process of developing and communicating an opinion about the quality of all or part of the work of another appraiser...* As such, proper identification of the subject of the review and the scope of work determines the extent and applicability of the requirements in Standards Rules 3-1, 3-2, and 3-3.

The following list is an outline of a real property appraisal review report completed in compliance with STANDARD 3 by an appraiser when the assignment does not include the reviewer providing an opinion of value.

Appraisal Review

The following items must be addressed in a Review Report of an appraisal prepared in accordance with Standards Rule 3-2 of USPAP if they are included in the scope of work of the assignment.

1. State identity of client, by name or type. [SR 3-2(a)]
2. State the intended user(s) of the review. [SR 3-2(a)]
3. State the intended use of the assignment results (client's use: quality control, audit, qualification, etc.). [SR 3-2(a)]
4. State the purpose of the assignment. [SR 3-2(a)]
5. State the information necessary to identify the subject of the review assignment; the property appraised; the property interest appraised; the effective date of the opinion in the work under review; the date of the review; and the appraiser(s) who completed the work under review, unless the identity was withheld. [SR 3-2(b), referring to 3-1(b)]
6. State the nature, extent, and detail of the review process undertaken (i.e., the scope of work). [SR 3-2(c), referring to SR 3-1(c)]
7. State the reviewer's opinion as to the completeness of the material under review within the scope of work applicable in the review assignment, i.e., type of report, etc. [SR 3-2(d), referring to 3-1(d)]
8. State the reviewer's opinion as to the apparent adequacy and relevance of the data and the propriety of any adjustments to the data, given the scope of work. [SR 3-2(d), referring to 3-1(e)]
9. State the reviewer's opinion as to the appropriateness of the appraisal methods and techniques used, given the scope of work, and the reasons for any disagreement. [SR 3-2(d), referring to SR 3-1(f)]
10. State the reviewer's opinion as to whether the analyses, opinions, and conclusions in the report under review are appropriate and reasonable, given the scope of work, and the reasons for any disagreement. [SR 3-2(d), referring to 3-1(g)]
11. Clearly and conspicuously state all extraordinary assumptions and hypothetical conditions connected with the reviewer's opinion of value; and state that their use might have affected the assignment results. [SR 3-2(d)]
12. Include all known pertinent information, i.e., information must be sufficient for users to understand rationale for reviewer's opinions and conclusions; include limiting conditions of the review, etc. [SR 3-2(e)]
13. Include a signed certification similar in content to SR 3-3. [SR 3-2(f)]

NOTE: An opinion of value by the reviewer that concurs with, or is different from, that in the work under review, or a statement that the value opinion in the work under review remains reasonable as of a more current effective date, may be expressed in the review report, provided the reviewer satisfies the requirements of STANDARD 1, 4, 6, 7, or 9 in developing that opinion; identifies and states any additional data relied upon and the reasoning and basis for the different opinion of value; and states all assumptions and limitations connected with the different opinion of value to avoid confusion in the marketplace. Items from the work under review may be incorporated by using an extraordinary assumption. (See STANDARD 3 and AO-20 for guidance.)

Discussion Examples: STANDARD 3

- A. A review appraiser with a busy litigation practice takes great delight in criticizing every work product he is handed, always citing USPAP violations. He proudly boasts of “never finding an appraisal he couldn’t tear apart.” He confidently prepares his USPAP critique before ever seeing the appraisal to be reviewed, then just drops in the facts. Discuss the potential issues relating to the appraisal review approach taken by this review appraiser.
- B. A reviewer for All-Purpose Bank has reviewed real property appraisals for many years. His supervisor has requested that he review an industrial appraisal that includes a substantial amount of fixtures and equipment in addition to the real estate.

What Standard should be used for this review? Does the **COMPETENCY RULE** apply in this case?

- C. Appraiser A, a state certified general appraiser, works as a staff appraiser/reviewer for the First of All Bank in Centertown. Her boss has asked her to review a Self-Contained Appraisal Report on the Peach Blossom Office Center prepared by Appraiser B, a fee appraiser. Appraiser A is to review the appraisal prepared by Appraiser B and provide the bank with her value opinion based on the contents of Appraiser B’s appraisal report. Appraiser A is uncertain whether she can accept this assignment without inspecting the subject and comparable properties, verifying the information in the report, and conducting her own, independent data search and analysis.

What is she required to do? How would her role and responsibilities change if the reporting option were a Restricted Use Appraisal Report? Would her responsibilities change if the client only wanted her to “concur or not concur” with the value?

- D. An appraisal reviewer for the Bank of Centerville prepares written reviews of commercial appraisals developed for the bank on properties with values in excess of \$1,000,000. The bank’s policies require all reviewers to comply with **STANDARD 3** and to reject any appraisal that is not within 5% of the reviewer’s opinion of value. Can an appraiser perform such a review assignment under USPAP? If so, what must the review appraiser do?

- E. A certified appraiser has been asked by a government agency to review two appraisals of the same real property and reconcile them to a single value. Can she perform this assignment under USPAP?
- F. A certified appraiser reviews many residential appraisals for a major lender. He has found numerous errors in several reports prepared by the same appraiser. He believes the errors are intentional and caused the value conclusions to be inflated in several instances. He has discussed the matter with his client but is also wondering if he is permitted by USPAP to file a complaint with the state appraiser board (where the appraiser is licensed) without his client's consent. Is he permitted to do so?

END OF SECTION



SECTION E

Uniform Standards of Professional Appraisal Practice: **STANDARDS 4 and 5—** **Real Property Appraisal Consulting, Development and Reporting**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 4 and its Standards Rules. See STANDARD 4, I–III; *Uniform Standards of Professional Appraisal Practice*, STANDARD 4, Standards Rules 4-1 and 4-2, including the Comments.
- Recognize that departure is not permitted from Standards Rules 4-1 and 4-2. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 4-1 and 4-2.
- Demonstrate familiarity with the topics addressed in STANDARD 5 and its Standards Rules. See STANDARD 5, I–IV; *Uniform Standards of Professional Appraisal Practice*, STANDARD 5, Standards Rules 5-1, 5-2, 5-3, and 5-4, including the Comments.
- Recognize that departure is not permitted from Standards Rules 5-1, 5-2, and 5-3. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 5-1, 5-2, and 5-3.
- Analyze examples to determine if a specific behavior violates the Standards Rules relating to STANDARDS 4 and 5 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARDS 4 and 5.

Uniform Standards of Professional Appraisal Practice: **STANDARDS 4 and 5—** **Real Property Appraisal Consulting, Development and Reporting**

The basic requirements for the development of a real property appraisal consulting assignment are presented in STANDARD 4, and the reporting requirements are presented in STANDARD 5. STANDARD 4 states: *In developing a real property appraisal consulting assignment, an appraiser must identify the problem to be solved and the scope of work necessary to solve the problem, and correctly complete the research and analysis necessary to produce credible results.* STANDARD 5 states: *In reporting the results of a real property appraisal consulting assignment, an appraiser must communicate each analysis, opinion, and conclusion in a manner that is not misleading.*

The Standards Rules related to STANDARDS 4 and 5 can be divided into two categories: binding requirements and specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in developing or reporting a properly supported value opinion. For example, whenever a specific requirement is necessary to the development of credible results, the appraiser must comply with the requirement. Invoking the DEPARTURE RULE is only necessary if a specific requirement is “applicable” to the assignment. (See the DEPARTURE RULE.) All portions of STANDARD 4 are binding. The binding requirements under STANDARD 5 are Standards Rules 5-1, 5-2, and 5-3. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

At the end of STANDARDS 4 and 5, use the Discussion Examples provided to explore the applications of the Standards Rules.

The definitions to the following terms should be reviewed in relation to STANDARDS 4 and 5:

Appraisal Consulting

Valuation Services

Appraisal Practice

Appraiser

Advocacy

Bias

Cost

Value

The Appraisal Standards Board periodically issues Advisory Opinions (AOs). The following Advisory Opinion should be studied in conjunction with this section:

Guidance:

AO-21: USPAP Compliance

STANDARD 4

I. Standards Rule 4-1 (Binding)

- A. This Standards Rule relates to the COMPETENCY RULE. Key points are:
 - 1. Recognized methods and techniques,
 - 2. Errors of omission and commission, and
 - 3. Careless and negligent practice.
- B. Note that this Standards Rule is identical in scope and intent to Standards Rule 1-1.

II. Standards Rule 4-2 (Binding)

- A. This Standards Rule is parallel to Standards Rule 1-2, in that it outlines the process to be undertaken in an appraisal consulting assignment.
- B. Standards Rule 4-2(c) is of particular importance, as it addresses the concept that every appraisal consulting assignment is centered on a problem to be solved.
- C. Standards Rule 4-2(f)(ii), concerning the scope of work necessary to ensure the credibility of the value opinion required as part of any appraisal consulting assignment, deserves special attention. Appraisers have three options in ensuring that credibility:
 - 1. If the value opinion is from a source other than the consulting appraiser, the value opinion may be reviewed in compliance with STANDARD 3, or
 - 2. The value opinion may be accepted as an extraordinary assumption, if all the requirements necessary to using such an assumption are fulfilled.
 - 3. If the consulting appraiser develops the necessary value opinion, the appraiser must develop that opinion in compliance with STANDARD 1.

- D. Standards Rules 4-2(g) and 4-2(h) describe the requirements necessary for using extraordinary assumptions and hypothetical conditions in appraisal consulting assignments. These are identical to the requirements set forth in Standards Rule 1-2. Be sure to note the requirement in Standards Rule 5-1(c) to *clearly and accurately disclose all assumptions, extraordinary assumptions, hypothetical conditions, and limiting conditions used in the assignment.*

III. Applicability of the DEPARTURE RULE

The DEPARTURE RULE does not apply to any part of STANDARD 4. After noting the similarities between Standards Rules 1-1 and 1-2 and Standards Rules 4-1 and 4-2, it should be clear why all portions of STANDARD 4 are binding. However, supplemental standards and/or jurisdictional exceptions may apply.

STANDARD 5

I. Standards Rule 5-1 (Binding)

The provisions of Standards Rule 5-1 are very similar to those of Standards Rule 2-1. In both cases, appraisers are required to report assignment results so that intended users can understand them and not be misled. The Comment to Standards Rule 5-1(c) requires that appraisal consulting reports include information adequate for intended users to understand both the reasoning and the analytical processes followed. The Comment also requires that *throughout the report the data, analyses, assumptions and conclusions are logical and adequately supported.*

II. Standards Rule 5-2 (Binding)

- A. Standards Rule 5-2 specifies the reporting levels required for various portions of appraisal consulting assignments. Standards Rule 5-2 closely parallels Standards Rule 3-2, in that it combines minimum levels of stating and summarizing information. Standards Rule 5-2(h) is critically important, in that it describes the requirements for reporting value opinions within appraisal consulting reports. If the value opinion comes from a source other than the consulting appraiser, there are three reporting options:

1. The information required under Standards Rule 3-2, or
2. A statement of the results of an appraisal review of that value opinion, plus a reference to appraisal review documentation in the appraisal consultant's workfile, or
3. A statement supporting the use of the appraisal as an extraordinary assumption.

- B. If the consulting appraiser develops the value opinion, that value opinion must be reported in the appraisal consulting report using the appropriate Self-Contained, Summary, or Restricted Use Appraisal Report option, shown in Standards Rule 2-2, excluding the Standards Rule 2-3 requirement as it is covered in the certification Standards Rule 5-2(j). Note that the Restricted Use Appraisal Report option is available if the client is the only intended user.

Standards Rule 5-2(j) requires a signed certification in all written appraisal consulting reports.

III. Standards Rule 5-3 (Binding)

Standards Rule 5-3 sets forth the content requirements for signed certifications within written appraisal consulting reports. Note here that advocacy is not permitted in appraisal consulting assignments. The language concerning contingent compensation also is the same as that in Standards Rule 2-3 and all the other certifications in USPAP.

IV. Standards Rule 5-4 (Departure Permitted)

Standards Rule 5-4 addresses the requirements for oral appraisal consulting reports, which are largely the same as those in Standards Rule 2-4 for oral appraisal reports.

V. Applicability of the DEPARTURE RULE

- A. Standards Rules 5-1, 5-2, and 5-3 are binding requirements. Therefore, the DEPARTURE RULE may not be applied to these three Standards Rules.
- B. Standards Rule 5-4 is a specific requirement, from which departure may be permitted, provided that Standards Rule 5-1 is adhered to and the requirements and specifications of the DEPARTURE RULE are followed.

Discussion Examples: STANDARDS 4 and 5

- A. A client asks an appraiser to review an appraisal report that was prepared by another appraiser. The client only wants an opinion of the quality of the original appraisal report, and does not want the appraiser to develop a separate value opinion. May the client's request be treated as an appraisal consulting assignment under **STANDARDS 4 and 5**?
- B. A real estate developer contacts a certified general appraiser and asks him to develop opinions as to the current market value of five different unit types that are being considered for a new development. In addition, the developer wants the appraiser to perform a market study to determine what mix of unit types would yield the fastest projected absorption rate. Which Standards apply?

- C. A client wants advice about how she might maximize her vacant warehouse property's potential. She engages the services of a state certified appraiser to develop a recommendation regarding whether she should demolish the improvement or redevelop it. Does the advice constitute an appraisal or an appraisal consulting assignment?
- D. An appraiser has been asked by a client to appear before the local Planning Board and assist him in obtaining a zoning change. The appraiser is to use an appraisal that the client has already had performed by another appraiser. The appraiser tells the client he will charge him by the hour for this service. Is this assignment an appraisal review, an appraisal consulting service, or a service that does not fall under USPAP? Is it okay to charge "by the hour," or is this practice considered some kind of contingent fee?
- E. Certified Appraiser A has accepted a tax consulting assignment and is to be compensated at one-half of the first year's tax savings. The appraiser completes the assignment, reporting his opinion of market value of the subject property for tax purposes. He clearly discloses his fee arrangement in the letter of transmittal, limiting conditions, and executive summary of his report and also includes a signed certification in accordance with **Standards Rule 5-3**. Is Appraiser A's fee arrangement in conformance with the Standards Rules? Why or why not?

If instead Appraiser A hires an independent appraiser to perform an appraisal for a fixed fee plus an hourly rate for testimony, and Appraiser A charges a contingent fee for presenting and managing the case, would this arrangement be allowed under USPAP? Why or why not?

- F. A client has asked real property Appraiser A at an appraisal firm to appraise five proposed model homes in a subdivision. Additionally, the client wants the appraiser to provide a market analysis and recommendations relating to current and proposed supply and demand, marketability, and financial feasibility of the models. The appraiser has the competency to perform the market study, but neither she nor others in the firm currently appraise single-family residences. However, she does know a residential appraiser who is qualified to perform the model home appraisals.

Can Appraiser A accept an assignment like this without appraising the model homes herself? If so, how would she complete it in compliance with USPAP and what are the reporting requirements?

- G. In an appraisal consulting assignment, does the consulting appraiser have to perform the appraisal, or can it come from another source?

END OF  SECTION

SECTION F

Uniform Standards of Professional Appraisal Practice: **STANDARD 6—** **Mass Appraisal, Development and Reporting**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 6 and its Standards Rules, including appraisal report options. See I-III; *Uniform Standards of Professional Appraisal Practice*, STANDARD 6, Standards Rules 6-1, 6-2, 6-3, 6-4, 6-5, 6-6, 6-7, and 6-8, including the Comments.
- Recognize that departure is not permitted from Standards Rules 6-1, 6-3, 6-6, 6-7, and 6-8. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 6-1, 6-3, 6-6, 6-7, and 6-8.
- Analyze examples to determine if a specific behavior violates the Standards Rules relating to STANDARD 6 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARD 6.

Uniform Standards of Professional Appraisal Practice: **STANDARD 6—** **Mass Appraisal, Development and Reporting**

The basic requirements for developing and reporting a mass appraisal are presented in STANDARD 6, which states: *In developing a mass appraisal, an appraiser must be aware of, understand, and correctly employ those recognized methods and techniques necessary to produce and communicate credible mass appraisals.* Eight Standards Rules follow this statement.

These Standards Rules can be divided into two categories: binding requirements and specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in developing or reporting a properly supported value opinion. For example, whenever a specific requirement is necessary to the development of credible results, the appraiser must comply with the requirement. Invoking the DEPARTURE RULE is only necessary if a specific requirement is “applicable” to the assignment. (See the DEPARTURE RULE.) The binding requirements under STANDARD 6 are Standards Rules 6-1, 6-3, 6-6, 6-7, and 6-8. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

At the end of STANDARD 6, use the Discussion Examples provided to explore the applications of the Standards Rules.

In studying STANDARD 6, the definitions of new terms used only in relation to this Standard are necessary.

Mass Appraisal

Mass Appraisal Model

NOTE: The following definitions are provided as supplementary information only. These two definitions are not from the DEFINITIONS section of USPAP.

Model Calibration: the process of analyzing sets of property and market data to determine the specific parameters of a model.

Model Specification: the formal development of a model in a statement or equation.

I. STANDARD 6

STANDARD 6 deals with the development of a mass appraisal, together with reporting the results of the mass appraisal process. In this regard, it is similar to STANDARD 3, which also covers both the development and reporting of an appraisal review.

- A. The Comment to STANDARD 6 indicates that it covers the substantive aspects of developing and communicating mass appraisals for both real property and personal property, whether for ad valorem or other purposes, and whether prepared with or without computer assistance.
1. The definition of *mass appraisal* is provided in the current edition of USPAP. This definition indicates that mass appraisal deals with a universe of properties, which are analyzed through:
 - a. Standard methodology, which implies that procedures are documented through reports and manuals,
 - b. Common data, which implies that data for sales and population available for the comparable sales are also available for the population or universe, and
 - c. Statistical testing, which implies a large enough sample or data set to produce reliable and statistically significant results.
 2. The method of mass appraisal can be appropriate for any appraisal assignment in which a universe of properties is valued.
 - a. Mass appraisal methods and techniques can be used to develop an appraisal of an individual property when the appraisal is performed in compliance with STANDARD 1 (real property) or STANDARD 7 (personal property).
 - b. USPAP indicates that a written report must be prepared and provided.
 3. When mass appraisal is applied to ad valorem property tax appraisals (which is its primary application), the JURISDICTIONAL EXCEPTION RULE may apply for some sections of STANDARD 6.
 - a. The appraiser engaging in mass appraisal for ad valorem property tax purposes, therefore, should carefully check and comply with applicable national, regional, and local laws.
 - b. Jurisdictional exceptions applicable to mass appraisal for ad valorem tax purposes do **not** apply to mass appraisals prepared for other (i.e., non-property tax) purposes.
 4. When the results of mass appraisals are tested or contested by single-property appraisals, those appraisals are not mass appraisals and therefore must conform to:
 - a. STANDARDS 1 and 2 for real property, and/or
 - b. STANDARDS 7 and 8 for personal property.

B. Standards Rule 6-1 (Binding)

Standards Rule 6-1 is identical in scope and content to Standards Rule 1-1, with the following additional items noted:

1. Standards Rule 6-1(a) emphasizes the critical importance of continuing education to maintain currency with mass appraisal methodology and procedures. This is an application of the COMPETENCY RULE.
2. The Comment to Standards Rule 6-1(a) identifies mass appraisal as a process that provides for *a systematic approach and uniform application of appraisal methods and techniques to obtain estimates of value that allow for statistical review and analysis of results*. This is what tends to set it apart from single-property appraisals.
3. Standards Rules 6-1(b) and (c) deal with errors and careless appraisals and are similar to Standards Rules 1-1(b) and (c).

C. Standards Rule 6-2 (Departure Permitted)

Standards Rule 6-2 is very similar to the list of requirements in Standards Rule 1-2, with the following additional items noted:

1. The Comment to Standards Rule 6-2 (c) does note that constraints on the mass appraisal process must not limit the scope of work to such a degree that the mass appraisal results are not credible.
2. The Comment to Standards Rule 6-2(g) states that the properties must be identified in general terms, and each individual property in the universe must be identified, with the information on its identity stored or referenced in its property record.
3. Standards Rule 6-2(i) states that, when the subject is real property, it is necessary to identify and consider any personal property, trade fixtures, or intangibles that are not real property but are included in the appraisal; and conversely, when the subject is personal property, it is necessary to identify and consider any real property or intangibles that are not personal property but are included in the appraisal.
4. The Comment to Standards Rule 6-2(i) also indicates that *mathematical extension* (i.e., simple addition, subtraction, or division) cannot be used to combine fractional parts to the whole, or to allocate the parts of the whole.
5. Standards Rule 6-2(j) requires consideration of the effect of existing land use regulations and the possibility of their being modified, as well as economic supply and demand. Avoid making *unsupported* conclusions regarding neighborhood decline, effective age, and so forth.

D. Standards Rule 6-3 (Binding)

Standards Rule 6-3 is somewhat similar to Standards Rule 1-3, with the following additional items noted:

1. Standards Rule 6-3(a) requires that the appraiser identify and consider appropriate market information.
2. Standards Rule 6-3(b) requires the use of generally recognized techniques such as the cost, sales comparison, and income approaches for specifying valuation models:
 - a. Tabular
 - b. Mathematical
 - c. Linear
 - d. Nonlinear
3. Standards Rule 6-3(b) indicates that proper techniques for specifying valuation models apply to both real property and personal property valuation models.
4. Standards Rule 6-3(c) covers ***recognized techniques for calibrating mass appraisal models***. (Bold added for emphasis)

Calibration is the process of ***analyzing sets of property and market data to determine the specific parameters of a model***. (Bold added for emphasis)
5. Calibration techniques for mass appraisal models include but are not limited to:
 - a. Multiple linear regression
 - b. Nonlinear regression
 - c. Adaptive estimation procedure

E. Standards Rule 6-4 (Departure Permitted)

The scope and intent of Standards Rule 6-4 are the same as those for Standards Rule 1-4, with the following additional items noted:

1. The Comment to Standards Rule 6-4(a) establishes standards for the quality and quantity of factual data necessary to produce credible appraisals.

- a. Standard forms and systems for routine collection and maintenance of data records should be established.
 - b. Cadastral map systems should be compiled *according to current standards of detail and accuracy*.
 - c. Property characteristics data that are contemporaneous with the date of sale should appear in the data file for each sale and population.
 - d. The property characteristics data file for the population should also include data contemporaneous with the date of appraisal.
 - e. The data collection (and editing) program *must incorporate a quality control program* to ensure current and consistent records.
2. Standards Rule 6-4(b) requires income, expense, and other projections to be based on reasonable and appropriate evidence. This is interrelated with SMT-2, *Discounted Cash Flow Analysis*.

F. Standards Rule 6-5 (Departure Permitted)

Standards Rule 6-5 deals with the application of a *calibrated mass appraisal model*. This is different from the requirements and specifications of STANDARD 1 or STANDARD 4.

1. Standards Rules 6-5(a) and (b) require the use of *recognized methods or techniques*. This requirement represents a further application of the COMPETENCY RULE and indicates the need for continuing education for the mass appraisal professional.
2. Standards Rule 6-5(c), which addresses leasehold and leased fee opinions, requires proper identification of the interest. Contract rents are too often confused with market rents.
3. Standards Rule 6-5(d) poses data collection problems for unique circumstances.
4. Standards Rule 6-5(e) suggests that proposed improvements (on- or off-site) may sometimes represent an integral part of a mass appraisal assignment. When they do, the provisions of SMT-4, *Prospective Value Opinions*, apply.

G. Standards Rule 6-6 (Binding)

Standards Rule 6-6 addresses the results of a mass appraisal.

1. Standards Rule 6-6(a) requires the appraiser to *reconcile the quality and quantity of data*. This binding requirement must not be ignored.

2. The Comment to Standards Rule 6-6(b) deals with ensuring that overall, the calibrated models produce *value conclusions that meet attainable standards of accuracy*. In statistical terms, this means reasonable, attainable levels of statistical reliability.
3. The Comment to Standards Rule 6-6(b) also identifies the responsibility of appraisers undertaking mass appraisal assignments to *evaluate the performance of models* through techniques such as the following:
 - a. Goodness-of-fit statistics
 - b. Hold-out samples
 - c. Analysis of residuals
 - d. Analysis of appraisal-to-sale ratio data

H. Standards Rule 6-7 (Binding)

Standards Rule 6-7 deals with reporting the results of a mass appraisal assignment.

1. A written report is required.
2. Documentation of a mass appraisal for ad valorem property tax purposes may be in many different forms.
3. The Comment to Standards Rule 6-7(f) specifies that whether a physical inspection of the properties was made *must be disclosed* as a *limiting condition* (in addition to the required certification statement included in Standards Rule 6-8).
4. The Comment to Standards Rule 6-7(k) indicates that a report for a mass appraisal for ad valorem property tax purposes should include a discussion of:
 - a. The rationale for each model used,
 - b. The calibration techniques used, and
 - c. The performance measures (tests of reliability and statistical significance, for example) used.
5. The Comment to Standards Rule 6-7(n) indicates that a report for a mass appraisal should address highest and best use requirements under statute law, case law, or public policy.
 - a. This may require application of the JURISDICTIONAL EXCEPTION RULE.

- b. When the requirement for valuation is actual use, the report *must discuss how **use-value** opinions were developed.* (Bold added for emphasis)
 - 6. Standards Rule 6-7(o) requires the appraiser to identify the appraisal performance tests used and set forth the performance measures attained.
 - 7. Standards Rule 6-7(p) requires the appraiser to describe the reconciliation performed, in accordance with Standards Rule 6-6.
- I. Standards Rule 6-8 (Binding)
- Standards Rule 6-8 specifies the certification required for all mass appraisal written reports and is similar to Standards Rule 2-3.
- 1. The form and content of the required certification are virtually identical with those specified in the other certifications in USPAP.
 - 2. There is a cross-reference to AO-2, *Inspection of the Subject Property Real Estate*, as guidance, with respect to any personal inspection of the property(ies) being appraised.
 - 3. The Comment to this Standards Rule states that the *certification is not intended to disturb an elected or appointed assessor's work plans or oaths of office. A signed certification is an integral part of the appraisal report. An appraiser, who signs any part of the mass appraisal report, including a letter of transmittal, must also sign this certification.*

II. Cross-References

- A. STANDARD 6 deals with **development and reporting** of the results of the mass appraisal process and, in that regard, is similar to STANDARD 3.
- B. Standards Rule 6-1 is virtually identical to Standards Rule 1-1.
- C. Standards Rule 6-2 is closely related to Standards Rule 1-2.
- D. Standards Rule 6-3 is similar to Standards Rule 1-3.
- E. Standards Rule 6-4 is similar to Standards Rule 1-4.
- F. Standards Rule 6-4(b) is interrelated with SMT-2, *Discounted Cash Flow Analysis*.
- G. Standards Rule 6-5(e) is interrelated with SMT-4, *Prospective Value Opinions*.
- H. Standards Rule 6-8 is similar to Standards Rule 2-3.
- I. Supplemental standards and/or jurisdictional exceptions may apply.

III. Applicability of the DEPARTURE RULE

- A. Standards Rules 6-2, 6-4, and 6-5 are specific requirements, from which departure may be permitted provided that the requirements and specifications of the DEPARTURE RULE are followed.
- B. Standards Rules 6-1, 6-3, 6-6, 6-7, and 6-8 are binding requirements. Therefore, the DEPARTURE RULE may not be applied to these five Standards Rules.

Discussion Examples: STANDARD 6

- A. An appraiser was recently hired as the assessor for the City of Junctionville and agreed to perform services under USPAP. Owner-initiated appeals in 2003 and 2004 revealed an increasing disparity and inequality in assessment ratios for some commercial properties. These commercial properties were valued using a cost-based model. A sales ratio study indicates performance standards at acceptable levels for all commercial property categories except hotels/motels and apartments. After analyzing the market, the appraiser determines that an income-based model is appropriate for these latter property types and converts the data into the new model. A second sales ratio study reveals that the newly created model results in acceptable performance standards. This new model produced increasing value changes from 30% to 40% for the hotels/motels and apartments, and is used in the 2005 assessment roll.

The owner of two apartment buildings is shocked when his properties' assessed values increased 35%. He appeals to the local hearing authority using appraisal reports prepared specifically for the case that indicate values of 20% less. The hearing authority reduces his assessments to the levels presented in his appraisals. In turn, the owner files a grievance with the City Council alleging the appraiser is incompetent and cites the income-based model she created as flawed. Given this information, did the appraiser violate USPAP?

- B. The tax day (effective date for assessments) of a township in a state is December 31, for the subsequent year. A property owner has asked the appraiser, who is the deputy assessor, to inspect his property December 1, 2004. He wants her to see that the addition started in October is not yet finished. The appraiser confirms the condition of the subject—the exterior is finished but the interior is still in the stud stage. The owner comments that no work would be done until he returns after New Year's. On December 23, the appraiser receives a final certificate of occupancy and confirmation from the building inspector that the addition is complete. She drives to the property and, although no one is home, can tell through the windows that the addition is complete. She leaves a note requesting that the owner call her to confirm the interior information.

On January 20, she has yet to receive a call from the owner. She reviews the plans and specifications on file and verifies information with the building inspector. She adds the characteristics to the 2005 assessment roll, noting on the property record card the date of inspection and that the interior elements are based on an extraordinary assumption. The owner subsequently files a complaint

with the assessor indicating he is being unfairly treated and the assessment should be based on the appraiser's December 1 physical inspection.

Did the appraiser violate USPAP when she added the addition as completed onto the assessment roll using an extraordinary assumption?

- C. A certified real estate appraiser with extensive experience in mass appraisal has recently begun contacting communities to inquire about providing appraisal services. A county equalization director has been contemplating having some of his communities appraised because they lack uniformity. He is interested in hiring the appraiser's company, but money is tight. The director tells the appraiser that if he can "guarantee" that the appraisal will increase values at least 20% and increase uniformity of assessment, he has the assignment. The appraiser indicates that he is confident he can meet those two objectives, so the director agrees to the terms. The director makes it very clear that the appraiser will only be paid if his appraisal results in the increases. The appraiser takes the assignment.

Is the appraiser violating USPAP by making such a "guarantee" in the assignment?

- D. The chief appraiser for a city assessor's office specifically prepares the annual values for all the commercial and industrial properties. State statute requires that the properties be appraised as if in fee simple. An owner of several multi-tenant properties in the city is appalled when he receives his assessment notices. He has owned the properties for over 15 years and some of his leases date back to the time he purchased the buildings. The owner calls the appraiser and learns the properties are being valued at market rent levels despite the fact that if he wanted to sell the buildings any purchaser would have to honor the existing lease contracts. The owner's complaint, filed with the city manager, states that the appraiser is not using the appropriate valuation methodologies and techniques for valuing his leased fee interest.

Did the appraiser violate USPAP by valuing the properties using market rent levels rather than contract rents?

- E. A retired city assessor decides to open an appraisal company and hires several staff people. His first assignment is with the City of Old Town to perform an appraisal of all its residential properties. The engagement agreement stipulates that the appraisal is to be finished within three years, is to be conducted using the city's mass appraisal software program, and is to be performed in compliance with USPAP. The scope of work identified included physically inspecting and measuring every home.

The appraiser is not familiar with the software program because it didn't come out until after he retired, but since every municipality in the county is now using it he feels it has to be good. He creates a record card for collecting data and splits his staff into two divisions, data collection and data entry. He spends two weeks training his staff in their respective duties.

Near the end of the third year, one of his staff discovers that the record cards being used don't include an area for basement finishes. Therefore, none of the inspecting staff have been identifying whether the properties they inspected had any basement finishes. Because they are out of time, the appraiser decides to simply let the mistake go and finish the project as they have been doing it.

Did the appraiser violate USPAP?



SECTION G

***Uniform Standards of Professional Appraisal Practice:* STANDARDS 7 and 8— Personal Property Appraisal, Development and Reporting**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 7 and its Standards Rules. See I; *Uniform Standards of Professional Appraisal Practice*, STANDARD 7, Standards Rules 7-1, 7-2, 7-3, 7-4, 7-5, and 7-6, including the Comments.
- Recognize that departure is not permitted from Standards Rules 7-1, 7-2, 7-5, and 7-6. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 7-1, 7-2, 7-5, and 7-6.
- Demonstrate familiarity with the topics addressed in STANDARD 8 and its Standards Rules. See II; *Uniform Standards of Professional Appraisal Practice*, STANDARD 8, Standards Rules 8-1, 8-2, 8-3, and 8-4, including the Comments.
- Recognize that departure is not permitted from Standards Rules 8-1, 8-2, and 8-3. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 8-1, 8-2, and 8-3.
- Analyze examples to determine if a specific behavior violates the Standards Rules relating to STANDARDS 7 and 8 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARDS 7 and 8.

Uniform Standards of Professional Appraisal Practice STANDARDS 7 and 8— Personal Property Appraisal, Development and Reporting

The basic requirements for the development of a personal property appraisal are presented in STANDARD 7, which states: *In developing a personal property appraisal, an appraiser must identify the problem to be solved and the scope of work necessary to solve the problem and correctly complete research and analysis necessary to produce a credible appraisal.* The reporting requirements are presented in STANDARD 8, which states: *In reporting the results of a personal property appraisal, an appraiser must communicate each analysis, opinion, and conclusion in a manner that is not misleading.*

The Standards Rules can be divided into two categories: binding requirements and specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in developing or reporting a properly supported value opinion. For example, whenever a specific requirement is necessary to the development of credible results, the appraiser must comply with the requirement. Invoking the DEPARTURE RULE is only necessary if a specific requirement is “applicable” to the assignment. (See the DEPARTURE RULE.) The binding requirements under STANDARD 7 are Standards Rules 7-1, 7-2, 7-5, and 7-6. The binding requirements under STANDARD 8 are Standards Rules 8-1, 8-2, and 8-3. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

At the end of STANDARDS 7 and 8, use the Discussion Examples provided to explore the applications of the Standards Rules.

The definition of the following term should be reviewed in relation to personal property appraisal.

Personal Property

The Appraisal Standards Board periodically issues Advisory Opinions for guidance on specific appraisal issues or problems. The following Advisory Opinions apply to this section (previously covered in Section D under STANDARD 2):

Guidance:

- AO-11: *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*
- AO-12: *Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2*

I. STANDARD 7

- A. *Personal property* is defined in the DEFINITIONS section of the current edition of USPAP.
- B. Personal property is both portable and tangible, as defined and used within USPAP. (*Intangible property* appraisal is addressed in STANDARD 9.)

Examples include, but are not limited to, the following:

1. Machinery and equipment
2. Furniture and fixtures
3. Trade fixtures
4. Artwork and antiques
5. Gems and jewelry
6. Collectibles

Simply put, personal property is all tangible property that is not classified as real property.

- C. Comparison with STANDARD 1

Most of STANDARD 7 is very similar to STANDARD 1 with regard to the topics covered, the location in which the topics are presented, and the specific handling of most topics.

The following will list the sections and specifically point out any significant differences. Differences will begin with the notation “DIFF.”

1. Standards Rule 7-1 (Binding)
Is similar to Standards Rule 1-1.
2. Standards Rule 7-2 (Binding)

DIFF—The Comment to Standards Rule 7-2(c)(iv) focuses on opinions of value *in a specified market or at a specified market level* rather than on the real estate issue of *market value* definition. In the appraisal of personal property, the particular market into which an item might be sold, and the level of that market, can have a significant impact on the value conclusion. The term *market value* is not as commonly used in personal property as it is in real property. Therefore, in this section, as well as in other sections to be pointed out in STANDARDS 7 and 8, the focus is different.

DIFF—The characteristics listed in Standards Rule 7-2(e)(i) through (iii) focus on the identification of the subject property a little differently. The identification, in terms of the authentication, of certain personal property items, such as antiques or works of art, can be an important part of the appraisal process for personal property. Similarly, this Standards Rule also focuses on the relative quality of the subject property and on other physical and economic characteristics that impact its value.

3. Standards Rule 7-3 (Departure Permitted)

DIFF—Standards Rule 1-3 is separated because it specifically addresses requirements when the type and definition of value is market value and discusses highest and best use issues. Standards Rule 7-3 does not deal with market value, but does discuss highest and best use issues. It also focuses, again, on special considerations of the specific measurable marketplaces that are key in the appraisal of personal property. The introductory section to Standards Rule 7-3 is dissimilar to that of Standards Rule 1-3, but is very similar to that of Standards Rules 7-4 and 1-4.

4. Standards Rule 7-4 (Departure Permitted)

Is similar to Standards Rule 1-4.

5. Standards Rule 7-5 (Binding)

Is similar to Standards Rule 1-5 (a) in that it requires analysis of current agreements of sale, etc.

DIFF—Standards Rule 7-5, however, treats the analysis of prior sales differently from its treatment in Standards Rule 1-5. Standards Rule 7-5 only requires the analysis of prior sales that *occurred within a reasonable and applicable time period, given the intended use and the type of property involved*.

6. Standards Rule 7-6 (Binding)

Is similar to Standards Rule 1-6.

C. Applicability of the DEPARTURE RULE

1. Standards Rules 7-3 and 7-4 are specific requirements, from which departure may be permitted provided that the requirements and specifications of the DEPARTURE RULE are followed.
2. Standards Rules 7-1, 7-2, 7-5, and 7-6 are binding requirements. Therefore, the DEPARTURE RULE may not be applied to these four Standards Rules.

II. STANDARD 8

A. Comparison with STANDARD 2

Most of STANDARD 8 is very similar to STANDARD 2 with regard to the topics covered, the location in which the topics are presented, and the specific handling of most topics.

The only differences relate to the sections of STANDARD 2 that focus on market value issues, which are replaced in STANDARD 8 with discussion of *marketplaces*, as noted above.

B. Applicability of the DEPARTURE RULE

1. Standards Rule 8-4 includes specific requirements, from which departure may be permitted provided the requirements and specifications of the DEPARTURE RULE are followed.
2. Standards Rules 8-1, 8-2, and 8-3, are binding requirements. Therefore, the DEPARTURE RULE may not be applied to these three Standards Rules.

On the following page is a chart summarizing the reporting requirements, which is adapted from Standards Rule 8-2 and AO-11, *Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2*.

Uniform Standards of Professional Appraisal Practice Standards Rule 8-2 Report Comparison Chart— Personal Property

The essential difference among the three options is in the use and application of the terms “describe,” “summarize,” and “state.” “Describe” is used to connote a comprehensive level of detail in the presentation of information. “Summarize” is used to connote a more concise presentation of information. “State” is used to connote the minimal presentation of information.

a) Self-Contained Appraisal Report	b) Summary Appraisal Report	c) Restricted Use Appraisal Report
i. state the identity of the client and any intended users, by name or type;	i. state the identity of the client and any intended users, by name or type;	i. state the identity of the client, by name or type;
ii. state the intended use of the appraisal;	ii. state the intended use of the appraisal;	ii. state the intended use of the appraisal;
iii. describe information sufficient to identify the property involved in the appraisal, including the physical and economic property characteristics relevant to the assignment;	iii. summarize information sufficient to identify the property involved in the appraisal, including the physical and economic property characteristics relevant to the assignment;	iii. state information sufficient to identify the property involved in the appraisal;
iv. state the property interest appraised;	iv. state the property interest appraised;	iv. state the property interest appraised;
v. state the type and definition of value and cite the source of the definition;	v. state the type and definition of value and cite the source of the definition;	v. state the type of value and cite the source of its definition;
vi. state the effective date of the appraisal and the date of the report;	vi. state the effective date of the appraisal and the date of the report;	vi. state the effective date of the appraisal and the date of the report;
vii. describe sufficient information to disclose to the client and any intended users of the appraisal the scope of work used to develop the appraisal;	vii. summarize sufficient information to disclose to the client and any intended users of the appraisal the scope of work used to develop the appraisal;	vii. state the extent of the process of collecting, confirming, and reporting data or refer to an assignment agreement retained in the appraiser's workfile, which describes the scope of work to be performed;
viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;	viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;	viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;
ix. describe the information analyzed, the appraisal procedures followed, and the reasoning that supports the analyses, opinions, and conclusions;	ix. summarize the information analyzed, the appraisal procedures followed, and the reasoning that supports the analyses, opinions, and conclusions;	ix. state the appraisal procedures followed, state the value opinion(s) and conclusion(s) reached, and reference the workfile;
x. state, as appropriate to the class of personal property involved, the use of the property existing as of the date of value and the use of the property reflected in the appraisal; and, when reporting an opinion of market value, describe the support and rationale for the appraiser's opinion of the highest and best use of the property;	x. state, as appropriate to the class of personal property involved, the use of the property existing as of the date of value and the use of the property reflected in the appraisal; and, when reporting an opinion of market value, summarize the support and rationale for the appraiser's opinion of the highest and best use of the property;	x. state, as appropriate to the class of personal property involved, the use of the property existing as of the date of value and the use of the property reflected in the appraisal; and, when reporting an opinion of market value, state the appraiser's opinion of the highest and best use of the property;
xi. state and explain any permitted departures from specific requirements of STANDARD 7 and the reason for excluding any of the usual valuation approaches; and	xi. state and explain any permitted departures from specific requirements of STANDARD 7, and the reason for excluding any of the usual valuation approaches; and	xi. state and explain any permitted departures from applicable specific requirements of STANDARD 7; state the exclusion of any of the usual valuation approaches; and state a prominent use restriction that limits use of the report to the client and warns that the appraiser's opinions and conclusions set forth in the report cannot be understood properly without additional information in the appraiser's workfile; and
xii. include a signed certification in accordance with Standards Rule 8-3.	xii. include a signed certification in accordance with Standards Rule 8-3.	xii. include a signed certification in accordance with Standards Rule 8-3.

Comments have not been included in this chart.

Discussion Examples: STANDARDS 7 and 8

- A. A new personal property appraiser specializes in antiques (properties over 100 years old). He is extremely busy and accepts an assignment from an attorney for an estate, which includes fine china, rare books, and artwork. He delivers a Summary Appraisal Report. The next day the attorney calls him fuming because he has never witnessed such sloppiness. He tells the appraiser that nowhere in his appraisal does he even mention the condition of the items that were appraised.

Is there a problem with the appraisal if condition isn't mentioned?

- B. For a \$500 fee, a well-respected senior appraiser with 20 years' experience agrees to provide a liquidation value to his client, an owner of a small manufacturing business.

The client is selling his factory building and is not sure whether he will sell the business or just liquidate his assets. He asked the appraiser to provide him with an opinion of what all the machinery and equipment would be worth if sold. The appraiser provides the client with a brief letter on his stationery stating that the machinery and equipment is worth, in the appraiser's opinion, about \$7,000.

Three days later, the factory burned, and the machinery and equipment were destroyed. The owner submitted a claim for his machinery and equipment in the amount of the insurance of \$65,000. The insurance company investigator obtains a copy of the appraiser's letter stating the machinery and equipment was worth \$7,000.

Has the appraiser violated any part of USPAP? Does his letter constitute an appraisal report?

- C. An appraiser of personal property received a call from a business agent of a well-known country and western singer who had recently died. He was asked to undertake an appraisal of a collection of guitars for use in an estate tax matter. The appraiser was given the date of death. A formal proposal was written outlining the scope of work and the amount of the fee and was signed by the agent.

The appraiser had experience with appraising musical instruments owned by various "big name performers" that had been sold as collector items. He had also kept abreast of the market by subscribing to publications and maintaining contacts with dealers and collectors.

Research of the market revealed data to support the value of vintage guitars, but there were no sales, either private or through auctions, of any instruments owned by the deceased singer. He arrived at his value opinion and delivered the report to the agent along with his fee statement. The agent argued that the values were too low and, based on the stature of the deceased singer, they should be worth "thousands and thousands more"; the appraiser replied that he had found no sales to substantiate the agent's claim.

The agent was unhappy and insisted the appraiser change his appraisal—the appraiser would not. Did the appraiser comply with USPAP?

- D. The owner and operator of an antique shop advertises that she offers appraisal services. An attorney has asked her to perform an appraisal of personal property for estate taxes, explaining that the estate was left to an only son. She accepts the assignment.

After inspecting the furniture, glass, china, silver, and other household contents, the appraiser completed the appraisal. In the report, she provided a short cover letter that simply stated she had performed the appraisal, identified the total marketable cash value, made an offer to buy the estate at the value given, and included her signature. Attached were 13 pages of inventory with short descriptions and individual values for each property.

Did the appraiser comply with USPAP?

END OF  SECTION

SECTION H

Uniform Standards of Professional Appraisal Practice: **STANDARDS 9 and 10—** **Business Appraisal, Development and Reporting**

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the topics addressed in STANDARD 9 and its Standards Rules. See I; *Uniform Standards of Professional Appraisal Practice*, STANDARD 9, Standards Rules 9-1, 9-2, 9-3, 9-4, and 9-5, including the Comments.
- Recognize that departure is not permitted from Standards Rules 9-1, 9-2, 9-3, and 9-5. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 9-1, 9-2, 9-3, and 9-5.
- Demonstrate familiarity with the topics addressed in STANDARD 10 and its Standards Rules. See II; *Uniform Standards of Professional Appraisal Practice*, STANDARD 10, Standards Rules 10-1, 10-2, 10-3, and 10-4, including the Comments.
- Recognize that departure is not permitted from Standards Rules 10-1, 10-2, and 10-3. See *Uniform Standards of Professional Appraisal Practice*, DEPARTURE RULE and Standards Rules 10-1, 10-2, and 10-3.
- Analyze examples to determine if a specific behavior violates Standards Rules relating to STANDARDS 9 and 10 and, if so, suggest how a violation might have been avoided. See Discussion Examples: STANDARDS 9 and 10.

Uniform Standards of Professional Appraisal Practice: **STANDARDS 9 and 10—** **Business Appraisal, Development and Reporting**

The basic requirements for developing a business appraisal are presented in STANDARD 9, which states: *In developing a business or intangible asset appraisal, an appraiser must identify the problem to be solved and the scope of work necessary to solve the problem and correctly complete the research and analysis steps necessary to produce a credible appraisal.* The reporting requirements are presented in STANDARD 10, which states: *In reporting the results of a business or intangible asset appraisal, an appraiser must communicate each analysis, opinion, and conclusion in a manner that is not misleading.*

The Standards Rules can be divided into two categories: binding requirements and specific requirements. Appraisers must adhere to binding requirements at all times. Specific requirements are lists of directives that appraisers *may be required to follow* in developing or reporting a properly supported value opinion. For example, whenever a specific requirement is necessary to the development of credible results, the appraiser must comply with the requirement. Invoking the DEPARTURE RULE is only necessary if a specific requirement is “applicable” to the assignment. (See the DEPARTURE RULE.) The binding requirements under STANDARD 9 are Standards Rules 9-1, 9-2, 9-3, and 9-5. The binding requirements under STANDARD 10 are Standards Rules 10-1, 10-2, and 10-3. Under the DEPARTURE RULE, an appraiser may accept an assignment that calls for something different from or less than the specific requirements, **provided that the other requirements of the DEPARTURE RULE are followed.**

At the end of STANDARDS 9 and 10, use the Discussion Examples provided to explore the applications of the Standards Rules.

In studying the material in this section, the definitions of several new terms used only in STANDARDS 9 and 10 are necessary.

Business Enterprise

Business Equity

Intangible Property (Intangible Assets)

I. STANDARD 9

A. Specific definitions

1. *Business enterprise*
2. *Business equity*

3. *Intangible property*

Intangible property is nonphysical and examples include, but are not limited to, the following:

- Franchises
- Trademarks
- Patents
- Copyrights
- Goodwill
- Equities
- Contracts

B. Comparison with STANDARD 1

Most of STANDARD 9 is very similar to STANDARD 1 with regard to the topics covered, the location in which the topics are presented, and the specific handling of most topics, although less so than for STANDARD 7.

The following will list the sections and specifically point out any significant differences. Differences will begin with the notation “DIFF.”

1. Standards Rule 9-1 (Binding)
2. Standards Rule 9-2 (Binding)

DIFF—The special treatment of opinions of *market value* found in Standards Rule 1-2(c) are not present in Standards Rule 9-2, or anywhere else in STANDARDS 9 and 10, because the term generally is not used in business or intangible asset appraisal. The most often used definition of value in appraising business interests and intangible assets is *fair market value*.

DIFF— The list of information needed to identify the subject property is less lengthy in Standards Rule 9-2, and focused on the ownership percentage interest and accompanying elements of control. Whether or not the subject interest is a controlling or non-controlling interest of the business enterprise is a major influence on value, and the appraisal of non-controlling interests is much more common in business appraisal than it is in real property appraisal.

3. Standards Rule 9-3 (Binding)

DIFF—Standards Rule 9-3 is specific to business enterprise appraisal.

- a. The Comment to Standards Rule 9-3 indicates that the appraiser under certain circumstances must consider whether continued operation of a business produces the highest appraisal results.
- b. The business appraiser must under certain circumstances consider, unless there are contrary provisions of law in the pertinent jurisdiction, whether liquidation of an operating business might result in a higher value.
- c. The *certain circumstance* under which (a) and (b) above *must* be done is the circumstance in which the subject equity interest has the ability to cause liquidation of the enterprise (i.e., the business equity being appraised represents a **controlling** interest).
- d. If liquidation is the appropriate premise for the appraisal, then assets may need to be appraised:
 - i. Under STANDARD 1, if the assets are real estate or real property, or
 - ii. Under STANDARD 7, if the assets are personal property.
- e. There is no concept of highest and best use commonly used in the appraisal of a business enterprise or intangible asset; therefore, this topic is not addressed here.

4. Standards Rule 9-4 (Departure Permitted)

- a. DIFF—Standards Rule 9-4 does not specifically list the cost, sales comparison, and income approaches and specific items that would need to be addressed in each. Rather, it states that:
 - i. The appraiser must consider all such approaches, and
 - ii. An approach need not be used if it is not applicable, regardless of the availability of data.

- b. DIFF—Standards Rule 9-4(b) contains factors very similar to those in Revenue Ruling 59-60, and states that they are to be addressed *when relevant*. The concept is similar to the list of items included in Standards Rules 1-4(d) through (h).
 - c. DIFF—Standards Rule 9-4(b) states that an appraiser must include in the analysis, when relevant, data regarding past sale of capital stock or other ownership interests in the business enterprise being appraised. No specific time period is given for the study of these prior sales, other than *when relevant*.
8. Standards Rule 9-5 (Binding)

Standards Rule 9-5 relates to the reconciliation process and is similar in intent and purpose to Standards Rule 1-6.

C. Applicability of the DEPARTURE RULE

- 1. Standards Rule 9-4 contains specific requirements, from which departure may be permitted provided the requirements and specifications of the DEPARTURE RULE are followed.
- 2. Standards Rules 9-1, 9-2, 9-3, and 9-5 are binding requirements. Therefore, the DEPARTURE RULE may not be applied to these four Standards Rules.

II. STANDARD 10

A. Comparison with STANDARD 2

- 1. Most of STANDARD 10 is similar to STANDARD 2. The topics covered, the location in which the topics are presented, and the specific handling of most topics are similar, although less so than for STANDARD 8.
- 2. There are certain key differences:
 - a. DIFF—STANDARD 10 contains only two reporting options, not three. The options are the Appraisal Report and the Restricted Use Appraisal Report. The requirements for the Appraisal Report match the extent of discussion required for the Summary Appraisal Report in STANDARD 2. Therefore, STANDARD 10 contains no option that is equivalent to a Self-Contained Appraisal Report.
 - b. DIFF—STANDARD 10, as in STANDARD 9, does not contain any special discussion related to market value or highest and best use, as these concepts typically are not found in business and intangible asset appraisal.

- c. DIFF—There is one difference in the certification language.

This Standards Rule contains no reference to a personal inspection of the property, as it is difficult to inspect intangible assets.

B. Applicability of the DEPARTURE RULE

1. Standards Rule 10-4 includes specific requirements, from which departure may be permitted provided that the requirements and specifications of the DEPARTURE RULE are followed.
2. Standards Rules 10-1, 10-2, and 10-3 are binding requirements. Therefore, the DEPARTURE RULE may not be applied to these three Standards Rules.

On the following page is a chart summarizing the reporting requirements, which is adapted from Standards Rule 10-2.

Uniform Standards of Professional Appraisal Practice Standards Rule 10-2 Report Comparison Chart— Business Appraisal

The essential difference between the two options is in the use and application of the terms “**summarize**” and “**state**.” “**Summarize**” is used to connote a more concise presentation of information than “**describe**.” “**State**” is used to connote the minimal presentation of information.

a) Appraisal Report	b) Restricted Use Appraisal Report
i. state the identity of the client and any intended users, by name or type;	i. state the identity of the client;
ii. state the intended use of the appraisal;	ii. state the intended use of the appraisal;
iii. summarize information sufficient to identify the business or intangible asset appraised;	iii. state information sufficient to identify the business or intangible asset appraised;
iv. state as relevant to the assignment, the extent to which the business interest or the interest in the intangible asset appraised contains elements of ownership control, including the basis for that determination;	iv. state as relevant to the assignment, the extent to which the business interest or the interest in the intangible asset appraised contains elements of ownership control, including the basis for that determination;
v. state the type and definition of value and cite the source of the definition;	v. state the type of value and cite the source of its definition;
vi. state the effective date of the appraisal and the date of the report;	vi. state the effective date of the appraisal and the date of the report;
vii. summarize sufficient information to disclose to the client and any intended users of the appraisal the scope of work used to develop the appraisal;	vii. state the extent of the process of collecting, confirming, and reporting data or refer to an assignment agreement retained in the appraiser’s workfile that describes the scope of work to be performed;
viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;	viii. clearly and conspicuously state all extraordinary assumptions and hypothetical conditions; and state that their use might have affected the assignment results;
ix. summarize the information analyzed, the appraisal procedures followed; and the reasoning that supports the analyses, opinions, and conclusions;	ix. state the appraisal procedures followed, state the value opinion(s) and conclusion(s) reached, and reference the workfile;
x. state and explain any permitted departures from specific requirements of STANDARD 9 and the reason for excluding any of the usual valuation approaches; and	x. state and explain any permitted departures from applicable specific requirements of STANDARD 9; state the exclusion of any of the usual valuation approaches; and state a prominent use restriction that limits use of the report to the client and warns that the appraiser’s opinions and conclusions set forth in the report cannot be understood properly without additional information in the appraiser’s workfile; and
xi. include a signed certification in accordance with Standards Rule 10-3.	xi. include a signed certification in accordance with Standards Rule 10-3.

Discussion Examples: STANDARDS 9 and 10

- A. An appraiser who is employed by a large accounting firm has been asked by an audit partner for a value based only on rules of thumb used in a specific industry. The audit partner intends to rely on the value as a “guideline valuation” for a buy-sell agreement. What should the appraiser do?
- B. A senior associate at an appraisal firm was talking to a client about a recently prepared appraisal report. After reviewing the report, the client remarked that the “legal mumbo jumbo” in the certification appeared to be unnecessary given that he is a non-lawyer and he is likely to be the only one who would ever read the report anyway. He said that all of the qualifications and representations on this page meant nothing to him and that he preferred that the language be dropped from the report altogether. The appraiser wants to satisfy the client if at all possible, but he is unsure whether the certification is optional or not. What should he do?
- C. A company had recently redeemed a retired director’s stock. However, no mention of any prior transaction in company stock is made in a later appraisal. You are reviewing the appraisal and wonder why no mention of the prior transaction was made, especially since the prior transaction was conducted at a price more than double the appraisal conclusion. Upon further analysis, you find that the prior transaction seems to be overpriced and the appraisal results seem appropriate. Does the appraisal comply with USPAP?
- D. In a highly competitive market, your client asks you to perform an appraisal. The intended use is to set the acquisition price of a competitor. The competitor is reluctant to give you the information you require, as confidentiality agreements are in place. Furthermore, the competitor is concerned that your client may not actually make the acquisition and would end up getting valuable insights into the competitor’s operations. You do not believe you have adequate information to complete the assignment. Your client says that is all the information you will get and they need your analysis to make an offer. What should you do?
- E. An appraiser has had two years of experience as a business valuer. He has had no experience in appraising tangible assets such as real estate or fixtures and equipment, but has never had a problem as he assigns out that work when he feels it is needed.

In this case, he is appraising 100% of a company that owns and operates three outdoor movie theaters. They are marginally profitable and he develops a rather low value for the chain. He accepted the book value of the equipment and, although the real estate was owned, he did not get appraisals. However, he clearly stated in his report that he assumed a market value rent for the facility according to usual appraisal procedures.

The client sold the company with the three theaters. The new buyer promptly sold off the equipment at an auction, filed for permits, and, six months later, sold the land to a developer for five times the amount for which the appraiser had

appraised the entire company and its assets. Has the appraiser performed within USPAP?

- F. A senior appraiser with five years of appraisal experience has been working with a firm partner with 12 years of experience on a business appraisal for estate tax purposes. The appraiser has reached a preliminary opinion of value. Having performed most of the analysis, he presents it to the partner who agrees that the appraisal is well supported and reasonable. They call the client to report their results.

The client is shocked at how high the value is and says, “It will never do!” The partner quickly offers to re-examine the analysis and get back to him. When they hang up, the partner looks over the work papers for five minutes and instructs the appraiser to change them and the report, to use only the method that gave the lowest value, and to ignore certain issues the appraiser believes to be important.

They discuss these issues for some time. The appraiser does not believe the altered value is reasonable. The partner angrily insists that the appraiser change the report. The appraiser does so, but removes his name from it. What USPAP issues are presented in this situation?

END OF SECTION



SECTION I

Uniform Standards of Professional Appraisal Practice: Statements and Advisory Opinions

Lesson Objectives

Participants will be able to

- Demonstrate familiarity with the Statements on Appraisal Standards that have not been previously discussed. See I.
- Demonstrate familiarity with the Advisory Opinions that have not been previously discussed. See II.

Uniform Standards of Professional Appraisal Practice: Statements and Advisory Opinions

I. Statements on Appraisal Standards

The Appraisal Standards Board (ASB) of The Appraisal Foundation issues Statements and Advisory Opinions from time to time.

Statements are specifically for the purpose of clarification, interpretation, explanation, or elaboration of USPAP and have the full weight of a Standards Rule.

As of December 31, 2004, the ASB of The Appraisal Foundation had issued 10 Statements (seven active), listed as follows:

Statements on Appraisal Standards

SMT-1	<i>Appraisal Review—Clarification of <u>Comment</u> on Standards Rule 3-1(g): Retired</i>
SMT-2	<i>Discounted Cash Flow Analysis</i>
SMT-3	<i>Retrospective Value Opinions</i>
SMT-4	<i>Prospective Value Opinions</i>
SMT-5	<i><u>Confidentiality</u> Section of the ETHICS RULE: Retired</i>
SMT-6	<i>Reasonable Exposure Time in Real Property and Personal Property Market Value Opinions</i>
SMT-7	<i>Permitted Departure from Specific Requirements in Real Property and Personal Property Appraisal Assignments</i>
SMT-8	<i>Electronic Transmission of Reports: Retired</i>
SMT-9	<i>Identification of the Client's Intended Use in Developing and Reporting Appraisal, Appraisal Review, or Appraisal Consulting Assignment Opinions and Conclusions</i>
SMT-10	<i>Assignments for Use by a Federally Insured Depository Institution in a Federally Related Transaction</i>

All of the Statements on Appraisal Standards have been reviewed previously in the course.

II. Advisory Opinions

Advisory Opinions are communications by the ASB that do not establish new standards or interpret existing standards. Advisory Opinions are issued to illustrate the applicability of appraisal standards in specific situations and to offer advice from the ASB for the resolution of appraisal issues and problems.

As of December 31, 2004, the ASB of The Appraisal Foundation had issued 27 Advisory Opinions (25 active), listed as follows:

Advisory Opinions (Guidance)

AO-1	<i>Sales History</i>
AO-2	<i>Inspection of Subject Property Real Estate</i>
AO-3	<i>Update of a Prior Assignment</i>
AO-4	<i>Standards Rule 1-5(b)</i>
AO-5	<i>Assistance in the Preparation of an Appraisal</i>
AO-6	<i>The Appraisal Review Function: Retired</i>
AO-7	<i>Marketing Time Opinions</i>
AO-8	<i>Market Value vs. Fair Value in Real Property Appraisals</i>
AO-9	<i>The Appraisal of Real Property That May Be Impacted by Environmental Contamination</i>
AO-10	<i>The Appraiser-Client Relationship: Retired</i>
AO-11	<i>Content of the Appraisal Report Options of Standards Rules 2-2 and 8-2</i>
AO-12	<i>Use of the Appraisal Report Options of Standards Rules 2-2 and 8-2</i>
AO-13	<i>Performing Evaluations of Real Property Collateral to Conform with USPAP</i>
AO-14	<i>Appraisals for Subsidized Housing</i>
AO-15	<i>Using the DEPARTURE RULE in Developing a Limited Appraisal</i>
AO-16	<i>Fair Housing Laws and Appraisal Report Content</i>
AO-17	<i>Appraisals of Real Property with Proposed Improvements</i>

- AO-18 *Use of an Automated Valuation Model (AVM)*
- AO-19 *Unacceptable Assignment Conditions in Real Property Appraisal Assignments*
- AO-20 *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*
- AO-21 *USPAP Compliance*
- AO-22 *Scope of Work in Market Value Appraisal Assignments, Real Property*
- AO-23 *Identifying the Relevant Characteristics of the Subject Property of a Real Property Appraisal Assignment*
- AO-24 *Normal Course of Business*
- AO-25 *Clarification of the Client in a Federally Related Transaction*
- AO-26 *Readdressing (Transferring) a Report to Another Party*
- AO-27 *Appraising the Same Property for a New Client*

END OF  SECTION

SECTION J

Uniform Standards of Professional Appraisal Practice: **Course Review**

Course Review

- A. History, Professionalism, Valuation Services and Appraisal Practice, the PREAMBLE, and Structure of the *Uniform Standards of Professional Appraisal Practice*
- B. DEFINITIONS and Rules
- C. STANDARDS 1 and 2
- D. STANDARD 3
- E. STANDARDS 4 and 5
- F. STANDARD 6
- G. STANDARDS 7 and 8
- H. STANDARDS 9 and 10
- I. Statements and Advisory Opinions

END OF  SECTION

APPENDIX I

Title XI—Real Estate Appraisal Reform Amendments

TITLE XI
REAL ESTATE APPRAISAL REFORM
AMENDMENTS
[12 U.S.C. 3331-3351]

The following is a compilation of Title XI of the Financial Institutions Recovery, Reform, and Enforcement Act of 1989, as amended.

TITLE XI—REAL ESTATE APPRAISAL REFORM AMENDMENTS [12 U.S.C. 3331-3351].

SEC. 1101. PURPOSE [12 U.S.C. 3331]

The purpose of this title is to provide that Federal financial and public policy interests in real estate related transactions will be protected by requiring that real estate appraisals utilized in connection with federally related transactions are performed in writing, in accordance with uniform standards, by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision.

SEC. 1102. ESTABLISHMENT OF APPRAISAL SUBCOMMITTEE OF THE FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL [12 U.S.C. 3310]

The Federal Financial Institutions Examination Council Act of 1978 (12 U.S.C. 3301 et seq.) is amended by adding at the end thereof the following new section:

SEC. 1011. ESTABLISHMENT OF APPRAISAL SUBCOMMITTEE

There shall be within the Council a subcommittee to be known as the 'Appraisal Subcommittee', which shall consist of the designees of the heads of the Federal financial institutions regulatory agencies. Each such designee shall be a person who has demonstrated knowledge and competence concerning the appraisal profession.

SEC. 1103. FUNCTIONS OF APPRAISAL SUBCOMMITTEE [12 U.S.C. 3332]

(a) *In general.* The Appraisal Subcommittee shall —

(1) monitor the requirements established by States for the certification and licensing of individuals who are qualified to perform appraisals in connection with federally related transactions, including a code of professional responsibility;

(2) monitor the requirements established by the Federal financial institutions regulatory agencies and the Resolution Trust Corporation with respect to —

(A) appraisal standards for federally related transactions under their jurisdiction, and

(B) determinations as to which federally related transactions under their jurisdiction require the services of a State certified appraiser and which require the services of a State licensed appraiser;

(3) maintain a national registry of State certified and licensed appraisers who are eligible to perform appraisals in federally related transactions; and

(4) transmit an annual report to the Congress not later than January 31 of each year which describes the manner in which each function assigned to the Appraisal Subcommittee has been carried out during the preceding year.

(b) *Monitoring and reviewing Foundation.* The Appraisal Subcommittee shall monitor and review the practices, procedures, activities, and organizational structure of the Appraisal Foundation.

SEC. 1104. CHAIRPERSON OF APPRAISAL SUBCOMMITTEE; TERM OF CHAIRPERSON; MEETINGS [12 U.S.C. 3333]

(a) *Chairperson.* The Council shall select the Chairperson of the subcommittee. The term of the Chairperson shall be 2 years.

(b) *Meetings; quorum; voting.* The Appraisal Subcommittee shall meet at the call of the Chairperson or a majority of its members when there is business to be conducted. A majority of members of the Appraisal Subcommittee shall constitute a quorum but 2 or more members may hold hearings. Decisions of the Appraisal Subcommittee shall be made by the vote of a majority of its members.

SEC. 1105. OFFICERS AND STAFF [12 U.S.C. 3334]

The Chairperson of the Appraisal Subcommittee shall appoint such officers and staff as may be necessary to carry out the functions of this title consistent with the appointment and compensation practices of the Council.

SEC. 1106. POWERS OF THE APPRAISAL SUBCOMMITTEE [12 U.S.C. 3335]

The Appraisal Subcommittee may, for the purpose of carrying out this title, establish advisory committees, hold hearings, sit and act at times and places, take testimony, receive evidence, provide information, and perform research, as the Appraisal Subcommittee considers appropriate.

SEC. 1107. PROCEDURES FOR ESTABLISHING APPRAISAL STANDARDS AND REQUIRING THE USE OF CERTIFIED AND LICENSED APPRAISERS [12 U.S.C. 3336]

Appraisal standards and requirements for using State certified and licensed appraisers in federally related transactions pursuant to this title shall be prescribed in accordance with procedures set forth in section 553 of title 5, United States Code, including the publication of notice and receipt of written comments or the holding of public hearings with respect to any standards or requirements proposed to be established.

SEC. 1108. STARTUP FUNDING [12 U.S.C. 3337]

(a) *In general.* For purposes of this title, the Secretary of the Treasury shall pay to the Appraisal Subcommittee a one-time payment of \$5,000,000 on the date of the enactment of this Act. Thereafter, expenses of the subcommittee shall be funded through the collection of registry fees from certain certified and licensed appraisers pursuant to section 1109 or, if required, pursuant to section 1122(b) of this title.

(b) *Additional funds.* Except as provided in section 1122(b) of this title, funds in addition to the funds provided under subsection (a) may be made available to the Appraisal Subcommittee only if authorized and appropriated by law.

(c) *Repayment of Treasury loan.* Not later than September 30, 1998, the Appraisal Subcommittee shall repay to the Secretary of the Treasury the unpaid portion of the \$5,000,000 paid to the Appraisal Subcommittee pursuant to this section.

SEC. 1109. ROSTER OF STATE CERTIFIED OR LICENSED APPRAISERS; AUTHORITY TO COLLECT AND TRANSMIT FEES [12 U.S.C. 3338]

(a) *In general.* Each State with an appraiser certifying and licensing agency whose certifications and licenses comply with this title, shall—

(1) transmit to the Appraisal Subcommittee, no less than annually, a roster listing individuals who have received a State certification or license in accordance with this title; and

(2) collect from such individuals who perform or seek to perform appraisals in federally related transactions, an annual registry fee of not more than \$25, such fees to be transmitted by the State agencies to the Council on an annual basis. Subject to the approval of the Council, the Appraisal Subcommittee may adjust the dollar amount of registry fees, up to a maximum of \$50 per annum, as necessary to carry out its functions under this title.

(b) *Use of amounts appropriated or collected.* Amounts appropriated for or collected by the Appraisal Subcommittee under this section shall be used—

(1) to maintain a registry of individuals who are qualified and eligible to perform appraisals in connection with federally related transactions;

(2) to support its activities under this title;

(3) to reimburse the general fund of the Treasury for amounts appropriated to and expended by the Appraisal Subcommittee during the 24-month startup period following the date of the enactment of this title; and

(4) to make grants in such amounts as it deems appropriate to the Appraisal Foundation, to help defray those costs of the foundation relating to the activities of its Appraisal Standards and Appraiser Qualification Boards.

SEC. 1110. FUNCTIONS OF THE FEDERAL FINANCIAL INSTITUTIONS REGULATORY AGENCIES RELATING TO APPRAISAL STANDARDS [12 U.S.C. 3339]

Each Federal financial institutions regulatory agency and the Resolution Trust Corporation shall prescribe appropriate standards for the performance of real estate appraisals in connection with federally related transactions under the jurisdiction of each such agency or instrumentality. These rules shall require, at a minimum — (1) that real estate appraisals be performed in accordance with generally accepted appraisal standards as evidenced by the appraisal standards promulgated by the Appraisal Standards Board of the Appraisal Foundation; and (2) that such appraisals shall be written appraisals. Each such agency or instrumentality may require compliance with additional standards if it makes a determination in writing that such additional standards are required in order to properly carry out its statutory responsibilities.

SEC. 1111. TIME FOR PROPOSAL AND ADOPTION OF STANDARDS [12 U.S.C. 3340]

Appraisal standards established under this title shall be proposed not later than 6 months and shall be adopted in final form and become effective not later than 12 months after the date of the enactment of this Act.

SEC. 1112. FUNCTIONS OF THE FEDERAL FINANCIAL INSTITUTIONS REGULATORY AGENCIES RELATING TO APPRAISER QUALIFICATIONS [12 U.S.C. 3341]

(a) *In general.* Each Federal financial institutions regulatory agency and the Resolution Trust Corporation shall prescribe, in accordance with sections 1113 and 1114 of this title, which categories of federally related transactions should be appraised by a State certified appraiser and which by a State licensed appraiser under this title.

(b) *Threshold level.* Each Federal financial institutions regulatory agency and the Resolution Trust Corporation may establish a threshold level at or below which a certified or licensed appraiser is not required to perform appraisals in connection with federally related transactions, if such agency determines in writing that such threshold level does not represent a threat to the safety and soundness of financial institutions.

(c) *GAO study of appraisals in connection with real estate related financial transactions below the threshold level.*—

(1) *Study required.* At the end of the 18-month period, and the end of the 36-month period, beginning on the date of the enactment of this subsection [October 29, 1992], the Comptroller General of the United States shall conduct a study on the adequacy and quality of appraisals or evaluations conducted in connection with real estate related financial transactions below the threshold level established under subsection (b), taking into account —

- (A) the cost to any financial institution involved in any such transaction;
- (B) the possibility of losses to the Bank Insurance Fund, the Savings Association Insurance Fund, or the National Credit Union Share Insurance Fund;
- (C) the cost to any customer involved in any such transaction; and
- (D) the effect on low-income housing.

(2) *Reports to Congress and the appropriate Federal financial institutions regulatory agencies.* Upon completing each of the studies required under paragraph (1), the Comptroller General shall submit a report on the Comptroller General's findings and conclusions with respect to such study to the Federal financial institutions regulatory agencies, the Committee on Banking, Finance and Urban Affairs of the House of Representatives, and the Committee on Banking, Housing, and Urban Affairs of the Senate, together with such recommendations for legislative or administrative action as the Comptroller General determines to be appropriate.

SEC. 1113. TRANSACTIONS REQUIRING THE SERVICES OF A STATE CERTIFIED APPRAISER [12 U.S.C. 3342]

In determining whether an appraisal in connection with a federally related transaction shall be performed by a State certified appraiser, an agency or instrumentality under this title shall consider whether transactions, either individually or collectively, are of sufficient financial or public policy importance to the United States that an individual who performs an appraisal in connection with such transactions should be a State certified appraiser, except that—

- (1) a State certified appraiser shall be required for all federally related transactions having a value of \$1,000,000 or more; and
- (2) 1-to-4 unit, single family residential appraisals may be performed by State licensed appraisers unless the size and complexity requires a State certified appraiser.

SEC. 1114. TRANSACTIONS REQUIRING THE SERVICES OF A STATE LICENSED APPRAISER [12 U.S.C. 3343]

All federally related transactions not requiring the services of a State certified appraiser shall be performed by either a State certified or licensed appraiser.

SEC. 1115. TIME FOR PROPOSAL AND ADOPTION OF RULES [12 U.S.C. 3344]

As appropriate, rules issued under sections 1113 and 1114 shall be proposed not later than 6 months and shall be effective upon adoption in final form not later than 12 months after the date of the enactment of this Act.

SEC. 1116. CERTIFICATION AND LICENSING REQUIREMENTS [12 U.S.C. 3345]

(a) *In general.* For purposes of this title, the term "State certified real estate appraiser" means any individual who has satisfied the requirements for State certification in a State or territory whose criteria for certification as a real estate appraiser currently meets the minimum criteria for certification issued by the Appraiser Qualification Board of the Appraisal Foundation.

(b) *Restriction.* No individual shall be a State certified real estate appraiser under this section unless such individual has achieved a passing grade upon a suitable examination administered by a State or territory that is consistent with and equivalent to the Uniform State Certification Examination issued or endorsed by the Appraiser Qualifications Board of the Appraisal Foundation.

(c) *Definition.* As used in this section, the term "State licensed appraiser" means an individual who has satisfied the requirements for State licensing in a State or territory.

(d) *Additional qualification criteria.* Nothing in this title shall be construed to prevent any Federal agency or instrumentality under this title from establishing such additional qualification criteria as may be necessary or appropriate to carry out the statutory responsibilities of such department, agency, or instrumentality.

(e) *Authority of the Appraisal Subcommittee.* The Appraisal Subcommittee shall not set qualifications or experience requirements for the States in licensing real estate appraisers, including a de minimus [sic] standard. Recommendations of the Subcommittee shall be nonbinding on the States.

SEC. 1117. ESTABLISHMENT OF STATE APPRAISER CERTIFYING AND LICENSING AGENCIES [12 U.S.C. 3346]

To assure the availability of State certified and licensed appraisers for the performance in a State of appraisals in federally related transactions and to assure effective supervision of the activities of certified and licensed appraisers, a State may establish a State appraiser certifying and licensing agency.

SEC. 1118. MONITORING OF STATE APPRAISER CERTIFYING AND LICENSING AGENCIES [12 U.S.C. 3347]

(a) *In general.* The Appraisal Subcommittee shall monitor State appraiser certifying and licensing agencies for the purpose of determining whether a State agency's policies, practices, and procedures are consistent with this title. The Appraisal Subcommittee and all agencies, instrumentalities, and federally recognized entities under this title shall not recognize appraiser certifications and licenses from States whose appraisal policies, practices, or procedures are found to be inconsistent with this title.

(b) *Disapproval by Appraisal Subcommittee.*—The Federal financial institutions regulatory agencies, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, and the Resolution Trust Corporation shall accept certifications and licenses awarded by a State appraiser certifying the licensing agency unless the Appraisal Subcommittee issues a written finding that—

- (1) the State agency fails to recognize and enforce the standards, requirements, and procedures prescribed pursuant to this title;
- (2) the State agency is not granted authority by the State which is adequate to permit the agency to carry out its functions under this title; or
- (3) decisions concerning appraisal standards, appraiser qualifications, and supervision of appraiser practices are not made in a manner that carries out the purposes of this title.

(c) *Rejection of State certifications and licenses.*

- (1) Opportunity to be heard or correct conditions. Before refusing to recognize a State's appraiser certifications or licenses, the Appraisal Subcommittee shall provide that State's certifying and licensing agency a written notice of its intention not to recognize the State's certified or licensed appraisers and ample opportunity to provide rebuttal information or to correct the conditions causing the refusal.
- (2) Adoption of procedures. The Appraisal Subcommittee shall adopt written procedures for taking actions described in this section.
- (3) Judicial review. A decision of the subcommittee under this section shall be subject to judicial review.

SEC. 1119. RECOGNITION OF STATE CERTIFIED AND LICENSED APPRAISERS FOR PURPOSES OF THIS TITLE [12 U.S.C. 3348]

(a) *Effective date for use of certified or licensed appraisers only.*—

(1) *In general.* Not later than December 31, 1992, all appraisals performed in connection with federally related transactions shall be performed only by individuals certified or licensed in accordance with the requirements of this title.

(2) *Extension of effective date.* Subject to the approval of the Council, the Appraisal Subcommittee may extend, until December 31, 1991, the effective date for the use of certified or licensed appraisers if it makes a written finding that a State has made substantial progress in establishing a State certification and licensing system that appears to conform to the provisions of this title.

a. Temporary waiver of appraiser certification or licensing requirements for State having scarcity of qualified appraisers. Subject to the approval of the Council, the Appraisal Subcommittee may waive any requirement relating to certification or licensing of a person to perform appraisals under this title if the Appraisal Subcommittee or a State agency whose certifications and licenses are in compliance with this title, makes a written determination that there is a scarcity of certified or licensed appraisers to perform appraisals in connection with federally related transactions in a State or in any geographical political subdivision of a State, leading to significant delays in the performance of such appraisals. The waiver terminates when the Appraisal Subcommittee determines that such significant delays have been eliminated.

(c) *Reports to State certifying and licensing agencies.* The Appraisal Subcommittee, any other Federal agency or instrumentality, or any federally recognized entity shall report any action of a State certified or licensed appraiser that is contrary to the purposes of this title, to the appropriate State agency for a disposition of the subject of the referral. The State agency shall provide the Appraisal Subcommittee or the other Federal agency or instrumentality with a report on its disposition of the matter referred. Subsequent to such disposition, the subcommittee or the agency or instrumentality may take such further action, pursuant to written procedures, it deems necessary to carry out the purposes of this title.

SEC. 1120. VIOLATIONS IN OBTAINING AND PERFORMING APPRAISALS IN FEDERALLY RELATED TRANSACTIONS [12 U.S.C. 3349]

(a) *Violations.* Except as authorized by the Appraisal Subcommittee in exercising its waiver authority pursuant to section 1119(b), it shall be a violation of this section—

(1) for a financial institution to seek, obtain, or give money or any other thing of value in exchange for the performance of an appraisal by a person who the institution knows is not a State certified or licensed appraiser in connection with a federally related transaction; and

(2) for the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, or the Resolution Trust Corporation to knowingly contract for the performance of any appraisal by a person who is not a State certified or licensed appraiser in connection with a real estate related financial transaction defined in section 1121(5) to which such association or corporation is a party.

(b) *Penalties.* A financial institution that violates subsection (a)(1) shall be subject to civil penalties under section 8(i)(2) of the Federal Deposit Insurance Act or section 206(k)(2) of the Federal Credit Union Act, as appropriate.

(c) *Proceeding.* A proceeding with respect to a violation of this section shall be an administrative proceeding which may be conducted by a Federal financial institutions regulatory agency in accordance with the procedures set forth in subchapter II of chapter 5 of title 5, United States Code.

SEC. 1121. DEFINITIONS [12 U.S.C. 3350]

For purposes of this title:

(1) *State appraiser certifying and licensing agency.* The term "State appraiser certifying and licensing agency" means a State agency established in compliance with this title.

(2) *Appraisal Subcommittee; subcommittee.* The terms "Appraisal Subcommittee" and "subcommittee" mean the Appraisal Subcommittee of the Federal Financial Institutions Examination Council.

(3) *Council.* The term "Council" means the Federal Financial Institutions Examinations Council.

(4) *Federally related transaction.* The term "federally related transaction" means any real estate-related financial transaction which —

(A) a federal financial institutions regulatory agency or the Resolution Trust Corporation engages in, contracts for, or regulates; and

(B) requires the services of an appraiser.

(5) *Real estate related financial transaction.* The term "real estate-related financial transaction" means any transaction involving —

(A) the sale, lease, purchase, investment in or exchange of real property, including interests in property, or the financing thereof;

(B) the refinancing of real property or interests in real property; and

(C) the use of real property or interests in property as security for a loan or investment, including mortgage-backed securities.

(6) *Federal financial institutions regulatory agencies.* The term "Federal financial institutions regulatory agencies" means the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporations, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the National Credit Union Administration.

(7) *Financial institution.* The term "financial institution" means an insured depository institution as defined in section 3 of the Federal Deposit Insurance Act or an insured credit union as defined in section 101 of the Federal Credit Union Act.

(8) *Chairperson.* The term "Chairperson" means the Chairperson of the Appraisal Subcommittee selected by the council.

(9) *Foundation.*—The terms "Appraisal Foundation" and "Foundation" means the Appraisal Foundation established on November 30, 1987, as a not for profit corporation under the laws of Illinois.

(10) *Written appraisal.*—The term "written appraisal" means a written statement used in connection with a federally related transaction that is independently and impartially prepared by a licensed or certified appraiser setting forth an opinion of defined value of an adequately described property as of a specific date, supported by presentation and analysis of relevant market information.

SEC. 1122. MISCELLANEOUS PROVISIONS [12 U.S.C. 3351]

(a) *Temporary practice.*

(1) *In general.* A State appraiser certifying or licensing agency shall recognize on a temporary basis the certification or license of an appraiser issued by another State if—

(A) the property to be appraised is part of a federally related transaction,

(B) the appraiser's business is of a temporary nature, and

(C) the appraiser registers with the appraiser certifying or licensing agency in the State of temporary practice.

(2) *Fees for temporary practice.* A State appraiser certifying or licensing agency shall not impose excessive fees or burdensome requirements, as determined by the Appraisal Subcommittee, for temporary practice under this subsection.

(b) *Reciprocity.* The Appraisal Subcommittee shall encourage the States to develop reciprocity agreements that readily authorize appraisers who are licensed or certified in one State (and who are in good standing with their State appraiser certifying or licensing agency) to perform appraisals in other States.

(c) *Supplemental funding.* Funds available to the Federal financial institutions regulatory agencies may be made available to the Federal Financial Institutions Examination Council to support the council's functions under this title.

(d) *Prohibition against discrimination.* Criteria established by the Federal financial institutions regulatory agencies, the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, and the Resolution Trust Corporation for appraiser qualifications in addition to State certification or licensing shall not exclude a certified or licensed appraiser for consideration for an assignment solely by virtue of membership or lack of membership in any particular appraisal organization.

(e) *Other requirements.* A corporation, partnership, or other business entity may provide appraisal services in connection with federally related transactions if such appraisal is prepared by individuals certified or licensed in accordance with the requirements of this title. An individual who is not a State certified or licensed appraiser may assist in the preparation of an appraisal if—

(1) the assistant is under the direct supervision of a licensed or certified individual; and

(2) the final appraisal document is approved and signed by an individual who is certified or licensed.

(f) *Studies.*

(1) *Study.* The Appraisal Subcommittee shall—

(A) conduct a study to determine whether real estate sales and financing information and data that is available to real estate appraisers in the States is sufficient to permit appraisers to properly estimate the values of properties in connection with federally related transactions; and

(B) study the feasibility and desirability of extending the provisions of this title to the function of personal property appraising and to personal property appraisers in connection with Federal financial and public policy interests.

(2) *Report.* The Appraisal Subcommittee shall—

(A) report its findings to the Congress with respect to the study described in paragraph (1)(A) no later than 12 months after the date of the enactment of this title, and

(B) report its findings with respect to the study described in paragraph (1)(B) to Congress not later than 18 months after the date of the enactment of this title.

SEC. 1123. EMERGENCY EXCEPTIONS FOR DISASTER AREAS [12 U.S.C. 3352]

(a) *In general.* Each Federal financial institutions regulatory agency may, by regulation or order, make exceptions to this title, and to standards prescribed pursuant to this title, for transactions involving institutions for which the agency is the primary Federal regulator with respect to real property located within a disaster area if the agency—

(1) makes the exception not later than 30 months after the date on which the President determines, pursuant to section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act, that a major disaster exists in the area and

(2) determines that the exception —

(A) would facilitate recovery from the major disaster, and

(B) is consistent with safety and soundness.

(b) *3-year limit on exceptions.* Any exception made under this section shall expire not later than 3 years after the date of the determination referred to in subsection (a)(1).

(c) *Publication required.* Any Federal financial institutions regulatory agency shall publish in the Federal Register a statement that —

(1) describes any exception made under this section; and

(2) explains how the exception—

(A) would facilitate recovery from the major disaster, and

(B) is consistent with safety and soundness.

(d) *Disaster area defined.* For the purposes of this section, the term "disaster area" means an area in which the President, pursuant to section 401 of the Robert T. Stafford Disaster Relief and Emergency Assistance Act, has determined that a major disaster exists.

APPENDIX II

Office of the Comptroller of the Currency

Independent Appraisal and Evaluation Functions, October 28, 2003

OCC Bulletin 94-55, Interagency Appraisal and Evaluation Guidelines,
October 22, 1994

**Office of the Comptroller of the Currency
Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of Thrift Supervision
National Credit Union Administration**

INDEPENDENT APPRAISAL AND EVALUATION FUNCTIONS

October 28, 2003

The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Office of Thrift Supervision (OTS), and the National Credit Union Administration (NCUA) (the agencies) are jointly issuing this statement to address concerns identified during examinations about the independence of the collateral valuation process. This statement applies to all real estate-related financial transactions originated or purchased by a regulated institution for its own portfolio or as assets held for sale. It provides further clarification of, and should be reviewed in conjunction with, the agencies' appraisal and real estate lending regulations¹ and the *Interagency Appraisal and Evaluation Guidelines* (Guidelines).²

An institution's board of directors is responsible for reviewing and adopting policies and procedures that establish and maintain an effective, independent real estate appraisal and evaluation program (program) for all of its lending functions. The real estate lending functions include commercial real estate mortgage departments, capital market groups, and asset securitization and sales units. These independence concerns include the risk that improperly prepared appraisals may undermine the integrity of credit underwriting processes. More broadly, an institution's lending functions should not have undue influence that might compromise the program's independence.

Selecting Individuals to Perform Appraisals or Evaluations

The Guidelines establish minimum standards for an effective program, including standards for selecting individuals who may perform appraisals or evaluations. Among other considerations, the selection criteria must provide for the independence of the individual performing the appraisal or evaluation. That is, the individual has neither a direct nor indirect, interest, financial or otherwise, in the property or transaction. Institutions also need to ensure that the individual selected is competent to perform the assignment. Consideration should be given to the

¹ OCC: 12 CFR 34, subparts C and D; FRB: 12 CFR 208 subpart E and appendix C, and 12 CFR 225 subpart G; FDIC: 12 CFR 323 and 12 CFR Part 365; OTS: 12 CFR Part 564, and 12 CFR 560.100, and 12 CFR 560.101; and NCUA: 12 CFR Part 722.5.

² The interagency guidelines may be found in: *Comptroller's Handbook for Commercial Real Estate and Construction Lending* for OCC; SR letter 94-55 for FRB; FIL-74-94 for FDIC; and Thrift Bulletin 55a for OTS. NCUA was not a party to the Guidelines; however, the NCUA applies the content to credit unions, when applicable.

individual's qualifications, experience, and educational background. Selection occurs when, based on an oral or written agreement, the individual accepts the assignment to appraise or evaluate a particular property. Moreover, appraisal or evaluation development work should not commence until the institution finalizes the selection process.

The agencies' appraisal regulations address appraiser independence and require that an institution, or its agent, directly engage the appraiser. The only exception to this requirement is that an institution may use an appraisal prepared for another financial services institution, provided that the institution determines that the appraisal conforms to the agencies' appraisal regulations and is otherwise acceptable. Independence is compromised when an institution uses an appraiser who is recommended by the borrower or allows the borrower to select the appraiser from the institution's list of approved appraisers.

Institutions may not use an appraisal prepared by an individual who was selected or engaged by a borrower. An institution's use of a borrower-ordered appraisal violates the agencies' appraisal regulations. Likewise, institutions may not use "readdressed appraisals" -- appraisal reports that are altered by the appraiser to replace any references to the original client with the institution's name. Altering an appraisal report in a manner that conceals the original client or intended users of the appraisal is misleading and violates the agencies' appraisal regulations and the Uniform Standards of Professional Appraisal Practice (USPAP).

It is also important to ensure that the program is safeguarded from internal influence and interference from an institution's loan production staff. Individuals independent from the loan production area should oversee the selection of appraisers and individuals providing evaluation services. The agencies recognize that it may not be possible or practical for small institutions to separate the collateral valuation and loan production processes. To ensure independence, loan officials, officers or directors with the responsibility for ordering appraisals and evaluations should not have sole approval authority for granting the loan request.

When selecting and engaging individuals, an institution needs to identify the assignment and order the appropriate appraisal or evaluation, as discussed in the Guidelines. To foster control and accountability, the agencies encourage an institution to use written engagement letters when ordering appraisals, especially for large, complex, or out-of-area commercial real estate properties. An institution should include a copy of the written engagement letter in the permanent loan file. An appraiser may also incorporate an engagement letter in the appraisal report. The engagement letter confirms that the assignment was made in a manner that complies with the institution's procedures and the agencies' regulations and Guidelines.

Appraisal and Evaluation Compliance Reviews

An institution's appraisal and evaluation program must maintain effective internal controls that promote compliance with program standards and the agencies' appraisal regulations and Guidelines. Internal controls should, among other criteria, confirm that appraisals and evaluations are reviewed by qualified and adequately trained individuals who are not involved in the loan production processes. The institution's standards for and the depth of such reviews should reflect the risk of the transaction and the process through which the appraisal or

evaluation is obtained. An institution should establish more in depth review procedures for appraisals of large, complex or out-of-area commercial real estate credits and for those appraisals and evaluations that are ordered by agents of the institution, such as loan brokers or another financial services institution.

Even in small institutions when absolute lines of independence cannot be achieved, effective internal controls should be implemented to ensure that no single person has sole authority to render credit decisions involving loans on which they ordered or reviewed the appraisal or evaluation. Further, lending officials, officers, or directors should abstain from any vote or approval involving loans for which they performed the appraisal or evaluation.

Supervisory Approach

Examiners will review an institution's standards of independence, taking into consideration the size of the institution and the nature and complexity of its real estate-related activities. Examiners will consider whether policies and procedures are comprehensive and applied uniformly to all units engaging in federally related transactions.

If an institution suspects that a licensed or certified appraiser is violating applicable laws or USPAP, or is otherwise engaging in other unethical or unprofessional conduct, the institution should make referrals directly to the appropriate state appraiser regulatory authorities. Examiners finding evidence of unethical or unprofessional conduct, including improperly prepared appraisals or evaluations and readdressed appraisals, should forward their findings and their recommendations to their supervisory office for appropriate disposition and referral to the state appraiser regulatory authority, as necessary. Institutions and institution-affiliated parties, including lenders, staff and fee appraisers, are reminded that they could be subject to enforcement actions, which include removal/prohibition orders, cease and desist orders, and civil money penalties, for violations of the agencies' appraisal and real estate lending regulations.



Comptroller of the Currency
Administrator of National Banks

Subject: Interagency Appraisal
and Evaluation Guidelines

Description: Distribution of Appraisal and
Evaluation Guidelines

TO: Chief Executive Officers of National Banks, Department and Division Heads, and
Examining Personnel

PURPOSE:

This issuance replaces Banking Circular 225 (Rev.) dated September 28, 1992. It transmits the revised real estate appraisal and evaluation guidelines issued jointly by the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS).

BACKGROUND:

The attached guidelines address supervisory matters related to real estate appraisals and evaluations used to support real estate-related financial transactions. The guidelines also provide guidance to examining personnel and federally regulated institutions about prudent appraisal and evaluation policies, procedures, practices, and standards. Finally, these guidelines will help to ensure an institution's compliance with Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) and Section 304 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA).

HIGHLIGHTS OF THE REVISED GUIDELINES:

The guidelines establish standards for an institution's selection of licensed or certified appraisers or persons who perform evaluations for them. These individuals must possess certain qualifications, such as the requisite training, education, expertise, competency, and independence.

The guidelines reflect revisions to the agencies' appraisal regulation which reduced the number of supervisory appraisal standards from 14 to five. In general, these five minimum appraisal standards require: 1) compliance with the Uniform Standards for Professional Appraisal Practice (USPAP); 2) written appraisal reports that are sufficiently informative to support the institution's lending decision; 3) analysis and reporting of deductions and discounts, when appropriate; 4) a market value estimate, as defined by this appraisal regulation, and 5) appraisals performed by State licensed or certified appraisers.

**OCC BULLETIN**

Comptroller of the Currency
Administrator of National Banks

Subject: Interagency Appraisal
and Evaluation Guidelines

Description: Distribution of Appraisal and
Evaluation Guidelines

The guidelines discuss recent revisions to USPAP by the Appraisal Standards Board (ASB). The USPAP now identifies two types of appraisal assignments (Complete or Limited) and three types of appraisal reports (Self-Contained, Summary or Restricted). The agencies' appraisal regulation and these guidelines do not prohibit the use of any appraisal assignment or appraisal report format. Ultimately, each institution must ensure that the completed appraisal report is adequate to underwrite the institution's lending decision.

There are 12 exemptions in the recently revised appraisal regulation. Three of these exemptions require evaluations prepared in accordance with these guidelines. The three exemptions are: (1) loans of \$250,000 or less; (2) business loans of \$1 million or less that do not depend upon the sale of real estate or rental income to repay the loan; and, (3) renewals and refinancings when the institution's collateral protection is not threatened by the transaction even when new funds are advanced; or when only closing costs are advanced.

Other issues discussed in the guidelines are use of USPAP's Departure Provision; content of an evaluation; use of valid appraisals or evaluations to support subsequent transactions; and use of effective internal controls to promote compliance with the real estate appraisal and evaluation program.

FOR FURTHER INFORMATION CONTACT: The office of the Chief National Bank Examiner, Credit and Management Policy Division, (202) 874-5170.

Jimmy F. Barton
Chief National Bank Examiner

Attachment

**Office of the Comptroller of the Currency
Federal Deposit Insurance Corporation
Federal Reserve Board
Office of Thrift Supervision**

Interagency Appraisal and Evaluation Guidelines

October 27, 1994

Purpose

The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of Thrift Supervision (OTS) (the agencies) are jointly issuing these guidelines, which supersede each of the agencies' appraisal and evaluation guidelines issued in 1992.¹ These guidelines address supervisory matters relating to real estate appraisals and evaluations used to support real estate-related financial transactions and provide guidance to examining personnel and federally regulated institutions about prudent appraisal and evaluations policies, procedures, practices, and standards.

Background

The XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) requires the agencies to adopt regulations on the preparation and use of appraisals by federally regulated financial institutions.² Such real estate appraisals are to be in writing and performed in accordance with uniform standards by an individual whose competency has been demonstrated and whose professional conduct is subject to effective State supervision.

Common agency regulations³ issued pursuant to Section 304 of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) also require each regulated institutions to adopt

¹ FRB: "Guidelines for Real Estate Appraisal and Evaluation Programs," September 28, 1992; OCC: BC-225, "Real Estate Appraisal and Evaluation Guidelines," September 28, 1992; FDIC: FIL-69-92, "Guidelines for Real Estate Appraisal and Evaluation Programs," September 30, 1992; OTS: Thrift Bulletin 55, "Real Estate Appraisal and Evaluation Guidelines," October 13, 1992.

² OCC: 12 CFR Part 34, subpart C; FRB: 12 CFR 208.18 and 12 CFR 225, subpart G; FDIC: 12 CFR 323; and OTS: 12 CFR Part 564.

³ OCC: 12 CFR 34, subpart D; FRB: 12 CFR Part 208, subpart C; FDIC: 12 CFR Part 365; and OTS: 12 CFR Parts 545 and 563.

and maintain written real estate lending policies that are consistent with safe and sound banking practices and that reflect consideration of the real estate lending guidelines attached to the regulation. The real estate lending guidelines state that a real estate lending program should include an appropriate real estate appraisal and evaluation program.

Supervisory Policy

An institution's real estate appraisal and evaluation policies and procedures will be reviewed as part of the examination of the institution's overall real estate-related activities. An institution's policies and procedures should be incorporated into an effective appraisal and evaluation program. Examiners will consider the institution's size and the nature of its real estate-related activities when assessing the appropriateness of its program.

When analyzing individual transactions, examiners will review an appraisal or evaluation to determine whether the methods, assumptions, and findings are reasonable and in compliance with the agencies' appraisal regulations, policies,⁴ supervisory guidelines, and the institution's policies. Examiners also will review the steps taken by an institution to ensure that the individuals who perform its appraisals and evaluations are qualified and are not subject to conflicts of interest. Institutions that fail to maintain a sound appraisal or evaluation program or to comply with the agencies' appraisal regulations, policies, or these supervisory guidelines will be cited in examination reports and may be criticized for unsafe and unsound banking practices. Deficiencies will require corrective action.

Appraisal and Evaluation Program

An institution's board of directors is responsible for reviewing and adopting policies and procedures that establish an effective real estate appraisal and evaluation program. The program should:

- Establish selection criteria and procedures to evaluate and monitor the ongoing performance of individuals who perform appraisals or evaluations;
- Provide for the independence of the person performing appraisals or evaluations;
- Identify the appropriate appraisal for various lending transactions;
- Establish criteria for contents of an evaluation;
- Provide for the receipts of the appraisal or evaluation report in a timely manner to facilitate the underwriting decision;
- Assess the validity or existing appraisals or evaluations to support subsequent transactions;

⁴ The appraisal guidance contained in the "Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans," November 7, 1991, generally applies to all transactions.

- Establish criteria for obtaining appraisals or evaluations for transactions that are otherwise exempt from the agencies' appraisal regulations; and
- Establish internal controls that promote compliance with these program standards.

Selection of Individuals Who May Perform Appraisals and Evaluations

An institution's program should establish criteria to select, evaluate, and monitor the performance of the individual(s) who performs a real estate appraisal or evaluation. The criteria should ensure that:

- The institution's selection process is non-preferential and unbiased;
- The individual selected possesses the requisite education, expertise and competence to complete the assignment;
- The individual selected is capable of rendering an unbiased opinion; and
- The individual selected is independent and has no direct or indirect interest, financial or otherwise, in the property or the transaction.

Under the agencies' appraisal regulations, the appraiser must be selected and engaged directly by the institution or its agent. The appraiser's client is the institution, not the borrower. An institution may use an appraisal that was prepared by an appraiser engaged directly by another financial services institution, as long as the institution determines that the appraisal conforms to the agencies' appraisal regulations and is otherwise acceptable.

Independent of the Appraisal And Evaluation Function

Because the appraisal and evaluation process is an integral component of the credit underwriting process, it should be isolated from influence by the institution's loan production process. An appraiser and an individual providing evaluation services should be independent of the loan and collection functions of the institution and have no interest, financial or otherwise, in the property or the transaction. If absolute lines of independence cannot be achieved, an institution must be able to clearly demonstrate that it has prudent safeguards to isolate its collateral evaluation process from influence or interference from the loan production process.

The agencies recognize, however, that it is not always possible or practical to separate the loan and collection functions from the appraisal or evaluation process. In some cases, such as in a small or rural institution or branch, the only individual qualified to analyze the real estate collateral may also be a loan officer, other officer, or director of the institution. To ensure their independence, such lending officials, officers, or directors should abstain from any vote or approval involving loans on which they performed an appraisal or evaluation.

Transactions That Require Appraisals

Although the agencies' appraisal regulations exempt certain categories of real estate-related financial transactions from the appraisal requirements, most real estate transactions over \$250,000 are considered federally related transactions and thus require appraisals.⁵ A "federally related transaction" means any real estate-related financial transaction in which the agencies engage, contract for, or regulate, and that requires the services of an appraiser. An agency also may impose more stringent appraisal requirements than the appraisal regulations require, such as when an institution's troubled condition is attributable to real estate loan underwriting problems.⁶

Minimum Appraisal Standards

The agencies' appraisal regulations include five minimum standards for the preparation of an appraisal. The appraisal must:

- Conform to generally accepted appraisal standards as evidenced by the Uniform Standards of Professional Appraisal Practice (USPAP) promulgated by the Appraisal Standards Board (ASB) of the Appraisal Foundation unless principles of safe and sound banking require compliance with stricter standards;

Although allowed by USPAP, the agencies' appraisal regulations do not permit an appraiser to appraise any property in which the appraiser has an interest, direct or indirect, financial or otherwise.

- Be written and contain sufficient information and analysis to support the institution's decision to engage in the transaction;

As discussed below, appraisers have available various appraisal development and report options; however, not all options may be appropriate for all transactions. A report option is acceptable under the agencies' appraisal regulations only if the appraisal report contains sufficient information and analysis to support an institution's decision to engage in the transaction.

⁵ In order to facilitate recovery in designated major disaster areas, subject to safety and soundness considerations, Section 2 of the Depository Institutions Disaster Relief Act of 1992 authorized the agencies to waive certain appraisal requirements for up to three years after a Presidential declaration of a natural disaster.

⁶ As a matter of policy, OTS requires problem associations and associations in troubled condition to obtain appraisals for all real estate-related transactions over \$100,000 (unless the transaction is otherwise exempt).

- Analyze and report appropriate deductions and discounts for proposed construction or renovation, partially leased buildings, non-market lease terms, and tract developments with unsold units;

This standard is designed to avoid having appraisals prepared using unrealistic assumptions and inappropriate methods. For federally related transactions, an appraisal is to include the current market value of the property in its actual physical condition and subject to the zoning in effect as of the date of the appraisal. For properties where improvements are to be constructed or rehabilitated, the regulated institution may also request a prospective market value based on stabilized occupancy or a value based on the sum of retail sales. However, the sum of retail sales for a proposed development is not the market value of the development for the purpose of the agencies' appraisal regulations. For proposed developments that involve the sale of individual houses, units, or lots, the appraiser must analyze and report appropriate deductions and discounts for holding costs, marketing costs and entrepreneurial profit. For proposed and rehabilitated rental developments, the appraiser must make appropriate deductions and discounts for items such as leasing commission, rent losses, and tenant improvements from an estimate based on stabilized occupancy.

- Be based upon the definition of market value set forth in the regulation; and

Each appraisal must contain an estimate of market value, as defined by the agencies' appraisal regulations.

- Be performed by State-licensed or certified appraisers in accordance with requirements set forth in the regulation.

Appraisal Options

An appraiser typically uses three market value approaches to analyze the value of a property—cost, income, and comparable sales—and reconciles the results of each to estimate market value. An appraisal will discuss the property's recent sales history and contain an opinion as to the highest and best use of the property. An appraiser must certify that he/she has compiled with USPAP and is independent. Also, the appraiser must disclose whether the subject property was inspected and whether anyone provided significant assistance to the person signing the appraisal report.

An institution may engage an appraiser to perform either a Complete or Limited Appraisal.⁷ When performing a Complete Appraisal assignment, an appraiser must comply with all USPAP standards without departing from any binding requirements and specific guidelines when estimating market value. When performing a Limited Appraisal, the appraiser elects to invoke the Departure Provision which allows the appraiser to depart, under limited conditions, from standards identified as specific guidelines. For example, in a Limited Appraisal, the appraiser might not utilize all three approaches to value. Departure from standards designated as binding requirements is not permitted.

An institution and appraiser must concur that use of the Departure Provision is appropriate for the transaction before the appraiser commences the appraisal assignment. The appraiser must ensure that the resulting appraisal report will not mislead the institution or other intended users of the appraisal report. The agencies do not prohibit the use of a Limited Appraisal for a federally related transaction, but the agencies believe that institutions should be cautious in their use of a Limited Appraisal because it will be less thorough than a Complete Appraisal.

Complete and Limited Appraisal assignments may be reported in three different report formats: a Self-Contained Report, a Summary Report, or a Restricted Report. The major difference among these three reports relates to the degree of detail presented in the report by the appraiser. The Self-Contained Appraisal Report provides the most detail, while the Summary Appraisal Report presents the information in a condensed manner. The Restricted Report provides a capsulized report with the supporting details maintained in the appraiser's files.

The agencies believe that the Restricted Report format will not be appropriate to underwrite a significant number of federally related transactions due to the lack of sufficient supporting information and analysis in the appraisal report. However, it might be appropriate to use this type of appraisal report for ongoing collateral monitoring of an institution's real estate transactions and under other circumstances when an institution's program requires an evaluation.

Moreover, since the institution is responsible for selecting the appropriate appraisal report to support its underwriting decisions, its program should identify the type of appraisal report that will be appropriate for various lending transactions. The institution's program should consider the risk, size, and complexity of the individual loan and the supporting collateral when determining the level of appraisal development and the type of report format that will be ordered. When ordering an appraisal report, institutions may want to consider the benefits of a written engagement letter that outlines the institution's expectations and delineates each party's responsibilities, especially for large, complex, or out-of-area properties.

⁷ USPAP Statement on Appraisal Standards No. 7 (SMT-7) — *Permitted Departure from Specific Guidelines for Real Property Appraisal*, issued March 30, 1994, effective July 1, 1994.

Transactions That Require Evaluations

A formal opinion of market value prepared by a State licensed or certified appraiser is not always necessary. Instead, less formal evaluations of the real estate may suffice for transactions that are exempt from the agencies' appraisal requirements. The agencies' appraisal regulations allow an institution to use an appropriate evaluation of the real estate rather than an appraisal when the transaction:

- Has a value of \$250,000 or less;
- Is a business loan of \$1,000,000 or less, and the transaction is not dependent on the sale of, or rental income derived from, real estate as the primary source of repayment; or
- Involves an existing extension of credit at the lending institution, provided that: (i) there has been no obvious and material change in the market conditions or physical aspects of the property that threaten the adequacy of the institution's real estate collateral protection after the transaction, even with the advancement of new monies; or (ii) there is no advancement of new monies other than funds necessary to cover reasonable closing costs.

Institutions should also establish criteria for obtaining appraisals or evaluations for safety and soundness reasons for transactions that are otherwise exempt from the agencies' appraisal regulations.

Evaluation Content

An institution should establish prudent standards for the preparation of evaluations. At a minimum, an evaluation should:

- Be written;
- Include the preparer's name, address, and signature, and the effective date of the evaluation;
- Describe the real estate collateral, its condition, its current and projected use;
- Describe the source(s) of information used in the analysis;
- Describe the analysis and supporting information, and;
- Provide an estimate of the real estate's market value, with any limiting conditions.

An evaluation report should include calculations, supporting assumptions, and, if utilized, a discussion of comparable sales. Documentation should be sufficient to allow an institution to understand the analysis, assumptions, and conclusions. An institution's own real estate loan portfolio experience and value estimate prepared for recent loans on comparable properties might provide a basis for evaluations.

An evaluation should provide an estimate of value to assist the institution in assessing the soundness of the transaction. Prudent practices also require that as an institution engages in more complex real estate-related financial transactions, or as its overall exposure increases, a more detailed evaluation should be performed. For example, an evaluation for a home equity loan might be based primarily on information derived from a sales data services organization or current tax assessment information, while an evaluation for an income-producing real estate property should fully describe the current and expected use of the property and include an analysis of the property's rental income and expenses.

Qualifications of Individuals Who Perform Evaluations

Individuals who prepare evaluations should have real estate-related training or experience and knowledge of the market relevant to the subject property. Based upon their experience and training, professionals from several fields may be qualified to prepare evaluations of certain types of real estate collateral. Examples include individuals with appraisal experience, real estate lenders, consultants or sales persons, agricultural extension agents, or foresters. Institutions should document the qualifications and experience level of individuals whom the institution deems acceptable to perform evaluations. An institution might also augment its in-house expertise and hire an outside party familiar with a certain market or a particular type of property. Although not required, an institution may use State licensed or certified appraisers to prepare evaluations. As such, Limited Appraisals reported in a Summary or Restricted format may be appropriate for evaluations of real estate-related financial transactions exempt from the agencies' appraisal requirements.

Valid Appraisals and Evaluations

The agencies allow an institution to use an existing appraisal or evaluation to support a subsequent transaction, if the institution documents that the existing estimate of value remains valid. Therefore, a prudent appraisal and evaluation program should include criteria to determine whether an existing appraisal or evaluation remains valid to support a subsequent transaction. Criteria for determining whether an existing appraisal or evaluation remains valid will vary depending upon the condition of the property and the marketplace, and the nature of any subsequent transaction. Factors that could cause changes to originally reported values include: the passage of time; the volatility of the local market; the availability of financing; the inventory of competing properties; improvements to, or lack of maintenance of, the subject property or competing surrounding properties; changes in zoning; or environmental contamination. The institution must document the information sources and analyses used to conclude that an existing appraisal or evaluation remains valid for subsequent transactions.

Renewals, Refinancings, and Other Subsequent Transactions

While the agencies' appraisal regulations generally allow appropriate evaluations of real estate collateral in lieu of an appraisal for loan renewals and refinancings, in certain situations an appraisal is required. If new funds are advanced over reasonable closing costs, an institution would be expected to obtain a new appraisal for the renewal of an existing transaction when there is a material change in market conditions or the physical aspects of the property that threatens the institution's real estate collateral protection.

The decision to reappraise or reevaluate the real estate collateral should be guided by the exemption for renewals, refinancings, and other subsequent transactions. Loan workouts, debt restructurings, loan assumptions, and similar transactions involving the addition or substitution of borrowers may qualify for the exemption for renewals, refinancings, and other subsequent transactions. Use of this exemption depends on the condition and quality of the loan, the soundness of the underlying collateral and the validity of the existing appraisal or evaluation.

A reappraisal would not be required when an institution advances funds to protect its interest in a property, such as to repair damaged property, because these funds should be used to restore the damaged property to its original condition. If a loan workout involves modification of the terms and conditions of an existing credit, including acceptance of new or additional real estate collateral, which facilitates the orderly collection of the credit or reduces the institution's risk of loss, a reappraisal or reevaluation may be prudent, even if it is obtained after the modification occurs.

An institution may engage in a subsequent transaction based on documented equity from a valid appraisal or evaluation, if the planned future use of the property is consistent with the use identified in the appraisal or evaluation. If a property, however, has reportedly appreciated because of a planned change in use of the property, such as rezoning, an appraisal would be required for a federally related transaction, unless another exemption applied.

Program Compliance

An institution's appraisal and evaluation program should establish effective internal controls that promote compliance with the program's standards. An individual familiar with the appropriate agency's appraisal regulation should ensure that the institution's appraisals and evaluations comply with the agencies' appraisal regulations, these guidelines, and the institution's program. Loan administration files should document this compliance review, although a detailed analysis or comprehensive analytical procedures are not required for every appraisal or evaluation. For some loans, the compliance review may be part of the loan officer's overall credit analysis and may take the form of either a narrative or a checklist. Corrective action should be undertaken for noted deficiencies by the individual who prepared the appraisal or evaluation.

An institution's appraisal and evaluation program should also have comprehensive analytical procedures that focus on certain types of loans, such as large-dollar credits, loans secured by complex or specialized properties, non-residential real estate construction loans, or out-of-area real estate. These comprehensive analytical procedures should be designed to verify that the methods, assumptions, and conclusions are reasonable and appropriate for the transaction and the property. These procedures should provide for a more detailed review of selected appraisals and evaluations prior to the final credit decision. The individual(s) performing these reviews should have the appropriate training or experience, and be independent of the transaction.

Appraisers and persons performing evaluations should be responsible for any deficiencies in their reports. Deficient reports should be returned to them for correction. Unreliable appraisals or evaluations should be replaced prior to the final credit decision. Changes to an appraisal's estimate of value are permitted only as a result of a review conducted by an appropriately qualified State licensed or certified appraiser in accordance with Standard III of USPAP.

Portfolio Monitoring

The institution should also develop criteria for obtaining reappraisals or reevaluations as part of a program of prudent portfolio review and monitoring techniques—even when additional financing is not being contemplated. Examples of such types of situations include large credit exposures and out-of-area loans.

Referrals

Financial institutions are encouraged to make referrals directly to state appraiser regulatory authorities when a State licensed or certified appraiser violates USPAP, applicable state law, or engages in other unethical or unprofessional conduct. Examiners finding evidence of unethical or unprofessional conduct by appraisers will forward their findings and recommendations to their supervisory office for appropriate disposition and referral to the state, as necessary.

APPENDIX III

Office of Management and Budget

OMB Bulletin No. 92-06, Guidance on Real Estate Appraisal Standards and Practices March 16, 1992

OMB Circular A-129, Issuance of Transmittal Memorandum Amending OMB Circular No. A-129, "Policies for Federal Credit Programs and Non-Tax Receivables," Notice, November 29, 2000



EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503
March 16, 1992

THE DIRECTOR

OMB BULLETIN NO. 92-06

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Guidance on Real Estate Appraisal Standards and Practices

1. **Purpose.** This Bulletin, which includes Attachments A and B, provides guidance to Federal agencies on standards and practices for real estate appraisals and real estate appraisal training.

2. **Background.** Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) (P.L. 101-73) establishes real estate appraisal requirements for federally regulated financial institutions. One requirement is that real estate appraisals must be conducted for all federally related real estate transactions. These real estate appraisals must be "performed in writing, in accordance with uniform standards, by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision."

OMB Circular A-129, "Managing Federal Credit Programs," as amended by OMB Bulletin 91-05, "Guidance for the Management of Guaranteed Loan Programs," adopted Title XI real estate appraisal standards for Federal credit programs. To ensure consistency with programs not covered by Circular A-129, this Bulletin extends Title XI real estate appraisal standards to certain agencies. These are agencies subject to the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (the Uniform Act), as amended, which was implemented by regulations in 49 CFR Part 24. In addition, this Bulletin directs agencies not subject to the Uniform Act to amend their real estate appraisal regulations to accord with 49 CFR Part 24.

3. **Effective Date.** This Bulletin becomes effective upon publication. Agencies seeking extension beyond the effective date must submit an implementation plan and schedule within one month of the date of publication of this Bulletin. This plan must be submitted to the Chief, Credit and Cash Management Branch, Office of Management and Budget.

Richard Darman
Director

Attachments

Attachment A

1. **General Policies.** All Federal agencies should follow the general policies listed below for real estate appraisals on Federal and federally assisted real estate transactions within their jurisdictions:

a. Federal agencies should establish criteria for, and identify real estate transactions requiring the use of, State-licensed or certified real estate appraisers.

b. Appraisers licensed or certified in States having laws, policies, and procedures in compliance with Title XI of FIRREA are qualified to prepare and review real estate appraisal reports for Federal agency programs.

c. Federal employees who choose to become State-licensed or certified real estate appraisers need only be licensed or certified in one State or territory to perform real estate appraisal duties as Federal employees in all States and territories.

d. Agencies should prepare real estate appraisal and appraiser review reports in accordance with written and approved agency standards consistent with the Uniform Standards of Professional Appraisal Practice (USPAP), sections I-III, as developed by the Appraisal Standards Board of the Appraisal Foundation.

2. **Implementation.** Agencies should revise regulations governing real appraisal qualifications and standards so that the regulations are in line with the general policies stated above, within six months from the date this Bulletin goes into effect.

a. The Department of Transportation has delegated to the Federal Highway Administration the authority to serve as lead agency under the Uniform Act. The Federal Highway Administration, in coordination with the Office of Management and Budget and the 17 affected eminent-domain agencies (Attachment B), should revise the implementing regulations of the Uniform Act, 49 CFR Part 24, in accordance with the guidance for real estate appraisal standards and practices established in this Bulletin.

b. Agencies not subject to the Uniform Act should follow the revised 49 CFR Part 24 in altering regulations to conform to the requirements of this Bulletin.

3. **Training.** Agencies should offer appropriate real estate appraisal training for employees who do or will perform State-licensed or certified real estate appraisals. The full course of

training should enable employees to achieve at least the minimum level of competence required by Title XI of FIRREA for State-licensed or certified real estate appraisers. The level achieved in this training should be consistent with the educational requirements established by the Appraisal Qualifications Board of the Appraisal Foundation.

4. **Reporting Requirements.** Within one month of the effective date of this Bulletin, the Chief Financial Officer of each agency, or the equivalent, will make a written report to the Chief, Credit and Cash Management Branch, Office of Management and Budget. The subject of the report will be the progress made in following the guidance in this Bulletin, as well as any major problems with compliance.

5. **Inquiries.** Inquiries and requests for assistance should be directed to the Chief, Credit and Cash Management Branch, Office of Management and Budget, telephone number (202) 395-3066.

Attachment B

Federal Agencies Covered by the Uniform Act

The Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (the Uniform Act) applies to the following Federal agencies:

Department of Agriculture
(7 CFR Part 21)

Department of Commerce
(15 CFR Part 11)

Department of Defense
(32 CFR Part 2509)

Department of Education
(34 CFR Part 15)

Department of Energy
(10 CFR Part 1039)

Environmental Protection
Agency
(40 CFR Part 4)

Federal Emergency Management
Agency
(44 CFR Part 25)

General Services
Administration
(41 CFR Part 105-51)

Department of Health and Human
Services
(45 CFR Part 15)

Department of Housing and
Urban Development
(24 CFR Part 42)

Department of the Interior
(41 CFR Part 114-50)

Department of Justice
(41 CFR Part 128-16)

Department of Labor
(29 CFR Part 12)

National Aeronautics and Space
Administration
(14 CFR Part 1208)

Pennsylvania Avenue
Development Corporation
(36 CFR Part 904)

Tennessee Valley Authority
(18 CFR Part 1306)

Department of Transportation
(49 CFR Part 24)

Department of Veterans Affairs
(38 CFR Part 25)



Federal Register

Wednesday,
November 29, 2000

Part III

Office of Management and Budget

Issuance of Transmittal Memorandum
Amending OMB Circular No. A-129,
“Policies for Federal Credit Programs and
Non-Tax Receivables”; Notice

OFFICE OF MANAGEMENT AND BUDGET
Issuance of Transmittal Memorandum Amending OMB Circular No. A-129, "Policies for Federal Credit Programs and Non-Tax Receivables"

AGENCY: Executive Office of the President, Office of Management and Budget, Budget Analysis and Systems Division.

ACTION: Notice of Transmittal amending OMB Circular No. A-129, "Policies for Federal Credit Programs and Non-Tax Receivables".

SUMMARY: This Circular updates policies and procedures for justifying, designing, and managing Federal credit programs and for collecting non-tax receivables.

FOR FURTHER INFORMATION CONTACT: Ms. Courtney Timberlake, Office of Management and Budget, Budget and Analysis Branch, NEOB Room 6001, 725 17th Street, NW, Washington, DC 20503, Tel. No. (202) 395-7864.

Availability: Copies of the OMB Circular A-129, and currently applicable Transmittal Memoranda may be obtained at the OMB Homepage on the Internet. The online address (URL) is <http://www.whitehouse.gov/OMB/circular/index.html#numerical>.

Dated: November 16, 2000.

Robert L. Nabors,

Executive Secretary and Assistant Director for Administration.

Policies For Federal Credit Programs and Non-Tax Receivables Circular No. A-129 (Revised)
OMB Circular No. A-129 (Revised) Policies for Federal Credit Programs and Non-Tax Receivables
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Executive Office of the President, Office of Management and Budget

Washington, DC 20503

Circular No. A-129

Revised

To the Heads of Executive Departments and Establishments

SUBJECT: Policies for Federal Credit Programs and Non-Tax Receivables

Federal credit programs are created to accomplish a variety of social and economic goals. Agencies must implement budget policies and management practices that ensure the goals of credit programs are met while properly identifying and controlling costs. In addition, Federal receivables, whether from credit programs or other non-tax sources, must be serviced and collected in an efficient and effective manner to protect the value of the Federal Government's assets.

General Information

1. *Purpose.* This Circular prescribes policies and procedures for justifying, designing, and managing Federal credit programs and for collecting non-tax receivables. It sets principles for designing credit programs, including: the preparation and review of legislation and regulations; budgeting for the costs of credit programs and minimizing unintended costs to the Government; and improving the efficiency and effectiveness of Federal credit programs. It also sets standards for extending credit, managing lenders participating in Government guaranteed loan programs, servicing credit and non-tax receivables, and collecting delinquent debt.

2. *Authority.* This Circular is issued under the authority of the *Budget and Accounting Act of 1921, as amended*; the *Budget and Accounting Act of 1950, as amended*; the

Debt Collection Act of 1982; as amended by the Debt Collection Improvement Act of 1996; Section 2653 of Public Law 98-369; the Federal Credit Reform Act of 1990, as amended; the Federal Debt Collection Procedures Act of 1990; the Chief Financial Officers Act of 1990, as amended; Executive Order 8248; the Cash Management Improvement Act Amendments of 1992; and pre-existing common law authority to charge interest on debts and to offset payments to collect debts administratively.

3. *Coverage. a. Applicability.* The provisions of this Circular apply to all credit programs of the Federal Government, including:

- (1) Direct loan programs;
- (2) Loan guarantee programs and loan insurance programs in which the Federal Government bears a legal liability to pay for all or part of the principal or interest in the event of borrower default; and
- (3) Loans or other financial assets acquired by a Federal agency (or a receiver or conservator acting for a Federal agency) as a result of a claim payment on a defaulted guaranteed or insured loan or in fulfillment of a Federal deposit insurance commitment.

Sections IV and V of Appendix A ("Managing the Federal Government's Receivables" and "Delinquent Debt Collection") also apply to receivables due to the Government from the sale of goods and services; fines, fees, duties, leases, rents, royalties, and penalties; overpayments to beneficiaries, grantees, contractors, and Federal employees; and similar debts.

b. *Exclusions Under the Debt Collection Acts.* Certain debt collection techniques authorized or mandated by the provisions of the Debt Collection Act of 1982 (DCA), as amended by the Debt Collection Improvement Act of 1996 (DCIA), do not apply to debts arising under the Internal Revenue Code, certain sections of the Social Security Act, or the tariff laws of the United States.

c. *Other Statutory Exclusions.* The policies and standards of this Circular do not apply when they are statutorily prohibited or are inconsistent with statutory requirements. However, agencies are required to periodically review legislation affecting the form of assistance and/or financial standards for credit programs to justify continuance of any non-conformance.

4. *Rescissions.* This Circular rescinds and replaces OMB Circular No. A-129 (revised), dated January 1993, and OMB Bulletin No. 91-05, dated November 26, 1990.

This Circular supplements, and does not supersede, the requirements applicable to budget submissions under OMB Circular No. A-11 and to proposed legislation and testimony under OMB Circular No. A-19.

5. *Effective Date.* This Circular is effective immediately.

6. *Inquiries.* Further information on the implementation of credit management and debt collection policies may be found in the Department of the Treasury's Financial Management Service Managing Federal Receivables and in OMB's Governmentwide 5-Year Plan for financial management submitted annually to Congress.

For inquiries concerning budget and legislative policy for credit programs contact

the Office of Management and Budget, Budget Review Division, Budget Analysis Branch, Room 6002, New Executive Office Building, 725 17th Street, NW, Washington, DC 20503; (202) 395-3945. Questions on all other sections of the Circular should be

directed to the Office of Federal Financial Management (202) 395-4534.

7. *Definitions.* Unless otherwise defined in this circular, key terms used in this circular are defined in OMB Circular Nos. A-11 and A-34.

Jacob J. Lew,

Director.

Appendices (3)

Appendix A to Circular No. A-129

I. Responsibilities of Departments and Agencies

REFERENCES

Statutory	Federal Credit Reform Act of 1990, 2 U.S.C. 661; Debt Collection Act of 1982/Debt Collection Improvement Act of 1996, 31 U.S.C. 3701, 3711-3720E; Federal Debt Collection Procedures Act of 1990; Budget and Accounting Act of 1921; Budget and Accounting Act of 1950; Chief Financial Officers Act of 1990; Cash Management Improvement Act Amendments of 1992;
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1. *Office of Management and Budget.* The Office of Management and Budget (OMB) is responsible for reviewing legislation to establish new credit programs or to expand or modify existing credit programs; monitoring agency conformance with the Federal Credit Reform Act; formulating and reviewing agency credit reporting standards and requirements; reviewing and clearing testimony pertaining to credit programs and debt collection; reviewing agency budget submissions for credit programs and debt collection activities; developing and maintaining the Federal credit subsidy calculator used to calculate the cost of credit programs; formulating and reviewing credit management and debt collection policy; approving agency credit management and debt collection plans; and providing training to credit agencies.

2. *Department of the Treasury.* The Department of the Treasury (Treasury), acting through the Office of Domestic Finance, works with OMB to develop Federal credit policies and/or reviewing legislation to create new credit programs or to expand or modify existing credit programs. The Department of the Treasury, through its Financial Management Service (FMS), promulgates government-wide debt collection regulations implementing the debt collection provisions of the *Debt Collection Improvement Act of 1996 (DCIA)*. FMS works with the Federal program agencies to identify debt that is eligible for referral to Treasury for cross-servicing and offset, and to establish target dates for referral. Performance measures are established which set annual referral and collection goals. In accordance with the DCIA and other Federal laws, FMS conducts offset of Federal payments, including tax refunds, under the Treasury Offset Program. FMS also provides collection services for delinquent non-tax Federal debts (referred to as cross-servicing), and maintains a private collection agency contract for referral and collection of delinquent debts. Additionally, FMS issues operational and procedural guidelines regarding government-wide credit management and debt collection such as "*Managing Federal Receivables*" and the "*Guide to the Federal Credit Bureau Program*." FMS, under its program responsibility for credit and debt management and as an active member of the Federal Credit Policy Working Group, assists in improving credit and debt management activities government-wide.

3. *Federal Credit Policy Working Group.* The Federal Credit Policy Working Group

(FCPWG) is an interagency forum that provides advice and assistance to the Office of Management and Budget (OMB) and Treasury in the formulation and implementation of credit policy. Membership consists of representatives from the Executive Office of the President, the Council of Economic Advisers, the OMB, and the Department of the Treasury. The major credit and debt collection agencies represented include the Departments of Agriculture, Commerce, Education, Health and Human Services, Housing and Urban Development, Interior, Justice, Labor, State, Transportation, Veterans Affairs and the Agency for International Development, the Export-Import Bank, the Federal Deposit Insurance Corporation and the Small Business Administration. Other departments and agencies may be invited to participate in the FCPWG at the request of the Chairperson. The Director of OMB designates the Chairperson of the FCPWG.

4. *Department and Agencies.* Departments and agencies shall manage credit programs and all non-tax receivables in accordance with their statutory authorities and the provisions of this Circular to protect the Government's assets and to minimize losses in relation to social benefits provided.

a. *Agencies shall ensure that:*

(1) Federal credit program legislation, regulations, and policies are designed and administered in compliance with the principles of this Circular;

(2) The costs of credit programs covered by the Federal Credit Reform Act of 1990 are budgeted for and controlled in accordance with the principles of that Act. (Some agencies and programs are expressly exempted from the statute.);

(3) Every effort is made to prevent future delinquencies by following appropriate screening standards and procedures for determination of creditworthiness;

(4) Lenders participating in guaranteed loan programs meet all applicable financial and programmatic requirements;

(5) Informed and cost effective decisions are made concerning portfolio management, including full consideration of contracting out for servicing or selling the portfolio;

(6) The full range of available techniques are used, such as those found in the Federal Claims Collection Standards and Treasury regulations, as appropriate, to collect delinquent debts, including demand letters, administrative offset, salary offset, tax refund offset, private collection agencies, cross-

servicing by Treasury, administrative wage garnishment, and litigation;

(7) Delinquent debts are written-off as soon as they are determined to be uncollectible; and

(8) Timely and accurate financial management and performance data are submitted to OMB and the Department of the Treasury so that the Government's credit management and debt collection programs and policies can be evaluated.

b. *In order to achieve these objectives, agencies shall:*

(1) Establish, as appropriate, boards to coordinate credit management and debt collection activities and to ensure full consideration of credit management and debt collection issues by all interested and affected organizations. Representation should include, but not be limited to, the agency Chief Financial Officer (CFO) and the senior official(s) for program offices with credit activities or non-tax receivables. The Board may seek from the agency's Inspector General, input based on findings and conclusions from past audits and investigations.

(2) Ensure that the statutory and regulatory requirements and standards set forth in this Circular, Treasury regulations, and supplementary guidance set forth in the Treasury/FMS Managing Federal Receivables are incorporated into agency regulations and procedures for credit programs and debt collection activities;

(3) Propose new or revised legislation, regulations, and forms as necessary to ensure consistency with the provisions of this Circular;

(4) Submit legislation and testimony affecting credit programs for review under the OMB Circular No. A-19 legislative clearance process, and budget proposals for review under the Circular No. A-11 budget justification process;

(5) Periodically evaluate Federal credit programs to assure their effectiveness in achieving program goals;

(6) Assign to the agency CFO, in accordance with the Chief Financial Officers Act of 1990, responsibility for directing, managing, and providing policy guidance and oversight of agency financial management personnel, activities, and operations, including the implementation of asset management systems for credit management and debt collection;

(7) Prepare, as part of the agency CFO Financial Management 5-Year Plan, a Credit

Management and Debt Collection Plan for effectively managing credit extension, account servicing, portfolio management and delinquent debt collection. The plan must ensure agency compliance with the standards in this Circular; and

(8) Ensure that data in loan applications and documents for individuals are managed in accordance with the Privacy Act of 1974, as amended by the Computer Matching and

Privacy Protection Act of 1988, and the Right to Financial Privacy Act of 1978, as amended. The Privacy Act of 1974 does not apply to loans and debts of commercial organizations.

II. Budget and Legislative Policy For Credit Programs

Federal credit assistance should be provided only when it is necessary and the

best method to achieve clearly specified Federal objectives. Use of private credit markets should be encouraged, and any impairment of such markets or misallocation of the nation's resources through the operation of Federal credit programs should be minimized.

1. Program Review

REFERENCES

Statutory	Federal Credit Reform Act of 1990, 2 U.S.C. 661.
Guidance	OMB Circular No. A-11.

Proposals submitted to OMB for new programs and for reauthorizing, expanding, or significantly increasing funding for existing credit programs should be accompanied by a written review which examines, at a minimum, the following factors:

a. The Federal objectives to be achieved, including:

(1) Whether the credit program is intended to:

(a) Correct a capital market imperfection, which should be defined; and/or

(b) Subsidize borrowers or other beneficiaries, who should be identified, or encourage certain activities, which should be specified.

(2) Why they cannot be achieved without Federal credit assistance, including:

(a) A description of existing and potential private sources of credit by type of institution and the availability and cost of credit to borrowers; and

(b) An explanation as to whether and why these private sources of financing and their terms and conditions must be supplemented and subsidized.

b. The justification for use of a credit subsidy. The review should provide an explanation of why a credit subsidy is the

most efficient way of providing assistance, including how it provides assistance in overcoming capital market imperfections, how it would assist the identified borrowers or beneficiaries or would encourage the identified activities, and why it would be preferable to other forms of assistance such as grants or technical assistance.

c. The estimated benefits of the program or program change. The review should estimate or, when the program exists, measure the benefits expected from the program or program change, including the amount by which the distribution of credit is expected to be altered and the favored activity is expected to increase. Information on conducting a cost-benefit analysis can be found in OMB Circular No. A-94.

d. The effects on private capital markets. The review should estimate the extent to which the program substitutes directly or indirectly for private lending, and analyze any elements of program design that encourage and supplement private lending activity, with the objective that private lending is displaced to the smallest degree possible by agency programs.

e. The estimated subsidy level. The review should provide an explicit estimate of the subsidy, as required by the Federal Credit

Reform Act of 1990, and an estimate of the expected annual administrative costs (including extension, servicing, and collection) of the credit program. If loan assets are to be sold or are to be included in a prepayment program for programmatic or other reasons, then the subsidy estimate should include the effects of the loan asset sales. For guidance on loan asset sales, see the Debt Collection Improvement Act of 1996, OMB Circular No. A-11, and the Treasury/FMS' Managing Federal Receivables. Loan asset sales/prepayment programs must be conducted in accordance with policies in this Circular and procedures in "Managing Federal Receivables," including the prohibitions against the financing of prepayments by tax-exempt borrowing and sales with recourse except where specifically authorized by statute. The cost of any guarantee placed on the asset sold requires budget authority.

f. The administrative resource requirements. The review should include an examination of the agency's current capacity to administer the new or expanded program and an estimation of any additional resources that would be needed.

2. Form of Assistance

REFERENCES

Statutory	Federal Credit Reform Act of 1990, 2 U.S.C. 661; Internal Revenue Code (Section 149(b)).
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When Federal credit assistance is necessary to meet a Federal objective, loan guarantees should be favored over direct loans, unless attaining the Federal objective requires a subsidy, as defined by the Federal Credit Reform Act of 1990, deeper than can be provided by a loan guarantee.

a. Loan guarantees may provide several advantages over direct loans. These advantages include: private sector credit servicing (which tends to be more efficient), private sector analysis of the borrowers creditworthiness, (which tends to allocate resources more efficiently), involvement of borrowers with private sector lenders (which promotes their movement to private credit), and lower portfolio management costs for agencies.

b. Loan guarantees, by removing part or all of the credit risk of a transaction, change the allocation of economic resources. Loan

guarantees may make credit available when private financial sources would not otherwise do so, or they may allocate credit to borrowers under more favorable terms than would otherwise be granted. This reallocation of credit may impose a cost on the Government and/or the economy.

c. Direct loans usually offer borrowers lower interest rates and longer maturities than loans available from private financial sources, even those with a Federal guarantee. The use of direct loans, however, may displace private financial sources and increase the possibility that the terms and conditions on which Federal credit assistance is offered will not reflect changes in financial market conditions. The costs to the Government and the economy are therefore likely to be greater.

d. Direct or indirect guarantees of tax-exempt obligations are prohibited under

Section 149(b) of the Internal Revenue Code. Guarantees of tax-exempt obligations are an inefficient way of allocating Federal credit. Assistance to the borrower, through the tax exemption and the guarantee, provides interest savings to the borrower that are smaller than the tax revenue loss to the Government. It is generally thought that the cost to the taxpayer is greater than the benefit to the borrower. The Internal Revenue Code provides some exceptions to this requirement; see Section 149(b) of the Internal Revenue Code for further details.

e. To preclude the possibility that Federal agencies will guarantee tax-exempt obligations, either directly or indirectly, agencies will:

(1) Not guarantee federally tax-exempt obligations;

(2) Provide that effective subordination of a direct or guaranteed loan to tax-exempt

obligations will render the guarantee void. To avoid effective subordination, the direct or guaranteed loan and the tax-exempt obligation should be repaid using separate dedicated revenue streams or otherwise separate sources of funding, and should be separately collateralized. In addition, the direct or guaranteed loan terms, such as grace periods, repayment schedules, and availability of deferrals, should be consistent with private sector standards to ensure that they do not create effective subordination;

(3) Prohibit use of a Federal guarantee as collateral to secure a tax-exempt obligation;

(4) Prohibit Federal guarantees of loans funded by tax-exempt obligations; and

(5) Prohibit the linkage of Federal guarantees with tax-exempt obligations. For example, such prohibited linkage occurs if the project is unlikely to be financed without the Federal guarantee covering a portion of the cost. In such cases, the Federal guarantee is, in effect, enabling the tax-exempt obligation to be issued, since without the

guarantee the project would not be viable to receive any financing. Therefore, the tax-exempt obligation is dependent on and linked to the Federal guarantee.

f. Where a large degree of subsidy is justified, comparable to that which would be provided by guaranteed tax-exempt obligations, agencies should consider the use of direct loans.

3. Financial Standards

REFERENCES

Statutory	Federal Credit Reform Act of 1990, 2 U.S.C. 661, Chief Financial Officers Act of 1990.
Guidance	OMB Circular No. A-11; SFFAS 2, OMB Circular No. A-34.

In accordance with the Federal Credit Reform Act of 1990, agencies must analyze and control the risk and cost of their programs. Agencies must develop statistical models predictive of defaults and other deviations from loan contracts. Agencies are required to estimate subsidy costs and to obtain budget authority to cover such costs before obligating direct loans and committing loan guarantees. Specific instructions for budget justification and subsidy cost estimation under the Federal Credit Reform Act of 1990 are provided in OMB Circular No. A-11, and instructions for budget execution are provided in OMB Circular No. A-34.

Agencies shall follow sound financial practices in the design and administration of their credit programs. Where program objectives cannot be achieved while following sound financial practices, the cost of these deviations shall be justified in agency budget submissions in comparison with expected benefits. Unless a waiver is approved, agencies should follow the financial practices discussed below.

a. Lenders and borrowers who participate in Federal credit programs should have a substantial stake in full repayment in accordance with the loan contract.

(1) Private lenders who extend credit that is guaranteed by the Government should bear at least 20 percent of the loss from a default. Loan guarantees that cover 100 percent of any losses on a loan encourage private lenders to exercise less caution than they otherwise would in evaluating loan requests. The level of guarantee should be no more than necessary to achieve program purposes. Loans for borrowers who are deemed to pose less of a risk should receive a lower guarantee.

(2) Borrowers should have an equity interest in any asset being financed with the credit assistance, and business borrowers should have substantial capital or equity at risk in their business (see Section III.A.3.b for additional discussion).

(3) Programs in which the Government bears more than 80 percent of any loss should be periodically reviewed to determine whether the private sector has become able to bear a greater share of the risk.

b. Agencies should establish interest and fee structures for direct loans and loan guarantees and should review these structures at least annually. Documentation

of the performance of these annual reviews for credit programs is considered sufficient to meet the review requirement described in Section 902(a)(8) of the Chief Financial Officers Act of 1990.

(1) Interest and fees should be set at levels that minimize default and other subsidy costs, of the direct loan or loan guarantee, while supporting achievement of the program's policy objectives.

(2) Agencies must request an appropriation in accordance with the Federal Credit Reform Act of 1990 for default and other subsidy costs not covered by interest and fees.

(3) Unless inconsistent with program purposes, and where authorized by law, riskier borrowers should be charged more than those who pose less risk. In order to avoid an unintended additional subsidy to riskier borrowers within the eligible class and to support the extension of credit to those riskier borrowers, programs that, for public policy purposes, do not adhere to this guideline, should justify the extra subsidy conveyed to the higher-risk borrowers in their annual budget submissions to OMB.

c. Contractual agreements should include all covenants and restrictions (e.g., liability insurance) necessary to protect the Federal Government's interest.

(1) Maturities on loans should be shorter than the estimated useful economic life of any assets financed.

(2) The Government's claims should not be subordinated to the claims of other creditors, as in the case of a borrower's default on either a direct loan or a guaranteed loan. Subordination increases the risk of loss to the Government, since other creditors would have first claim on the borrower's assets.

d. In order to minimize inadvertent changes in the amount of subsidy, interest rates to be charged on direct loans and any interest supplements for guaranteed loans should be specified by reference to the market rate on a benchmark Treasury security rather than as an absolute level. A specific fixed interest rate should not be cited in legislation or in regulation, because such a rate could soon become outdated, unintentionally changing the extent of the subsidy.

(1) The benchmark financial market instrument should be a marketable Treasury security with a similar maturity to the direct loans being made or the non-Federal loans being guaranteed. When the rate on the

Government loan is intended to be different than the benchmark rate, it should be stated as a percentage of that rate. The benchmark Treasury security must be cited specifically in agency budget justifications.

(2) Interest rates applicable to new loans should be reviewed at least quarterly and adjusted to reflect changes in the benchmark interest rate. Loan contracts may provide for either fixed or floating interest rates.

e. Maximum amounts of direct loan obligations and loan guarantee commitments should be specifically authorized in advance in annual appropriations acts, except for mandatory programs exempt from the appropriations requirements under Section 504(c) of the Federal Credit Reform Act of 1990.

f. Financing for Federal credit programs should be provided by Treasury in accordance with the Federal Credit Reform Act of 1990. Guarantees of the timely payment of 100 percent of the loan principal and interest against all risk create a debt obligation that is the credit risk equivalent of a Treasury security. Accordingly, a Federal agency other than the Department of the Treasury may not issue, sell, or guarantee an obligation of a type that is ordinarily financed in investment securities markets, as determined by the Secretary of the Treasury, unless the terms of the obligation provide that it may not be held by a person or entity other than the Federal Financing Bank (FFB) or another Federal agency. In *exceptional* circumstances, the Secretary of the Treasury may waive this requirement with respect to obligations that the Secretary determines: (1) Are not suitable for investment for the FFB because of the risks entailed in such obligations; or (2) are, or will be, financed in a manner that is least disruptive of private finance markets and institutions; or (3) are, or will be, based on the Secretary's consultation with OMB and the guaranteeing agency, financed in a manner that will best meet the goals of the program. The benefits of using the FFB must not expand the degree of subsidy.

g. Federal loan contracts should be standardized where practicable. Private sector documents should be used whenever possible, especially for loan guarantees.

4. Implementation

REFERENCES

Statutory	Federal Credit Reform Act of 1990, 2 U.S.C. 661; Government Performance and Results Act of 1993.
Guidance	OMB Circular No. A-11; OMB Circular No. A-19.

The provisions of this Section II will be implemented through the OMB Circular No. A-19 legislative review process and the OMB Circular No. A-11 budget justification and submission process. For accounting standards for Federal credit programs, see Accounting for Direct Loans and Loan Guarantees, Statement of Federal Financial Accounting Standards Number 2, developed by the Federal Accounting Standards Advisory Board.

a. Proposed legislation on credit programs, reviews of credit proposals made by others, and testimony on credit activities submitted by agencies under the OMB Circular No. A-19 legislative review process should conform to the provisions of this Circular.

Whenever agencies propose provisions or language not in conformity with the policies of this Circular, they will be required to request in writing that OMB waive the requirement. The request will be submitted on a standard waiver request form, available from OMB. Such requests will identify the waiver(s) requested, and will state the reasons for the request and the time period for which the exception is required. Exceptions, when allowed, will ordinarily be

granted only for a limited time in order to allow for an evaluation by OMB. The waiver request form should be submitted to the OMB examiner with primary responsibility for the account.

b. A checklist for reviews of legislative and budgetary proposals is included as Appendix B to this Circular. Agencies should use the model bill language provided in Appendix C in developing and reviewing legislation unless OMB has approved the use of alternative language that includes the same substantive elements.

c. Every four years, or more often at the request of the OMB examiner with primary responsibility for the account, the agency's annual budget submission (required by OMB Circular No. A-11, Section 15.2) should include:

(1) A plan for periodic, results-oriented evaluations of the effectiveness of the program, and the use of relevant program evaluations and/or other analyses of program effectiveness or causes of escalating program costs. A program evaluation is a formal assessment, through objective measurement and systematic analysis, addressing the manner and extent to which credit programs

achieve intended objectives. This information should be contained in agencies' annual performance plans submitted to OMB. (For further detail on program evaluation, refer to the Government Performance and Results Act of 1993 (GPRA) and related guidance);

(2) A review of the changes in financial markets and the status of borrowers and beneficiaries to verify that continuation of the credit program is required to meet Federal objectives, to update its justification, and to recommend changes in its design and operation to improve efficiency and effectiveness; and

(3) Proposed changes to correct those cases where existing legislation, regulations, or program policies are not in conformity with the policies of this Section II. When an agency does not deem a change in existing legislation, regulations, or program policies to be desirable, it will provide a justification for retaining the non-conformance.

III. Credit Management and Extension Policy

A. Credit Extension Policies

REFERENCES

Statutory	31 U.S.C. 3720B, 18 U.S.C. 1001, 31 U.S.C. 7701(d).
Regulatory	31 CFR 285.13, Executive Order 13109, 61 Federal Register 51763.
Guidance	Treasury/FMS "Managing Federal Receivables," "Treasury Report on Receivables (TROR)," and "Guide to the Federal Credit Bureau Program".

1. *Applicant Screening.* a. *Program Eligibility.* Federal credit granting agencies and private lenders in guaranteed loan programs, shall determine whether applicants comply with statutory, regulatory, and administrative eligibility requirements for loan assistance. If it is consistent with program objectives, borrowers should be required to certify and document that they have been unable to obtain credit from private sources. In addition, application forms must require the borrower to certify the accuracy of information being provided. (False information is subject to penalties under 18 U.S.C. 1001.)

b. *Delinquency on Federal Debt.* Agencies should determine if the applicant is delinquent on any Federal debt, including tax debt. Agencies should include a question on loan application forms asking applicants if they have such delinquencies. In addition, agencies and guaranteed loan lenders, shall use credit bureaus as a screening tool. Agencies are also encouraged to use other appropriate databases, such as the Department of Housing and Urban Development's Credit Alert Interactive Voice Response System CAIVRS to identify delinquencies on Federal debt.

Processing of applications shall be suspended when applicants are delinquent on Federal tax or non-tax debts, including judgment liens against property for a debt to the Federal Government, and are therefore not eligible to receive Federal loans, loan guarantees or insurance. (See 31 U.S.C. 3720B regarding non-tax debts.) This provision does not apply to disaster loans. Agencies should review and comply with 31 U.S.C. 3720B and 31 CFR 285.13 before extending credit. Processing should continue only when the debtor satisfactorily resolves the debts (e.g., pays in full or negotiates a new repayment plan).

c. *Creditworthiness.* Where creditworthiness is a criterion for loan approval, agencies and private lenders shall determine if applicants have the ability to repay the loan and a satisfactory history of repaying debt. Credit reports and supplementary data sources, such as financial statements and tax returns, should be used to verify or determine employment, income, assets held, and credit history.

d. *Delinquent Child Support.* Agencies shall deny Federal financial assistance to individuals who are subject to administrative offset to collect delinquent child support payments. See Executive Order 13109, 61

Federal Register 51763 (1996). The Attorney General has issued Minimum Due Process Guidelines: Denial of Federal Financial Assistance Pursuant to Executive Order 13109, which agencies shall include in their procedures or regulations promulgated for the purpose of denying Federal financial assistance in accordance with Executive Order 13109.

e. *Taxpayer Identification Number.* Pursuant to 31 U.S.C. 7701(d), agencies must obtain the taxpayer identification number (TIN) of all persons doing business with the agency. All agencies and lenders extending credit shall require the applicant or borrower to supply a TIN as a prerequisite to obtaining credit or assistance.

2. *Loan Documentation.* Loan origination files should contain loan applications, credit bureau reports, credit analyses, loan contracts, and other documents necessary to conform to private sector standards for that type of loan. Accurate and complete documentation is critical to providing proper servicing of the debt, pursuing collection of delinquent debt, and in the case of guaranteed loans, processing claim payments. Additional information on documentation requirements is available in

the supplement to the *Treasury Financial Manual Managing Federal Receivables*.

3. *Collateral Requirements.* For many types of loans, the Government can reduce its risk of default and potential losses through well managed collateral requirements.

a. *Appraisals of Real Property.* Appraisals of real property serving as collateral for a direct or guaranteed loan must be conducted in accordance with the following guidelines:

(1) Agencies should require that all appraisals be consistent with the Uniform Standards of Professional Appraisal Practice, promulgated by the Appraisal Standards Board of the Appraisal Foundation. Agencies shall prescribe additional appraisal standards as appropriate.

(2) Agencies should ensure that a State licensed or certified appraiser prepares an appraisal for all credit transactions over \$100,000 (\$250,000 for business loans).

(This does not include loans with no cash out and those transactions where the collateral is not a major factor in the decision to extend credit).

Agencies shall determine which of these transactions, because of the size and/or

complexity, must be performed by a State licensed or certified appraiser. Agencies may also designate direct or guaranteed loan transactions under \$100,000 (\$250,000 for business loans) that require the services of a State licensed or certified appraiser.

b. *Loan to Value Ratios.* In some credit programs, the primary purpose of the loan is to finance the acquisition of an asset, such as a single family home, which then serves as collateral for the loan. Agencies should ensure that borrowers assume an equity interest in such assets in order to reduce defaults and Government losses. Federal agencies should explicitly define the components of the loan to value ratio (LTV) for both direct and guaranteed loan programs. Financing should be limited by not offering terms (including the financing of closing costs) that result in an LTV equal to or greater than 100 percent. Further, the loan maturity should be shorter than the estimated useful economic life of the collateral.

c. *Liquidation of Real Property Collateral for Guaranteed Loans.* In general, it is not in the Federal Government's financial interest to assume the responsibility for managing

and disposing of real property serving as collateral on defaulted guaranteed loans. Private lenders should be required to liquidate, through litigation if necessary, any real property collateral for a defaulted guaranteed loan before filing a default claim with the credit granting agency.

d. *Asset Management Standards and Systems.* Agencies should establish policies and procedures for the acquisition, management, and disposal of real property acquired as a result of direct or guaranteed loan defaults. Agencies should establish inventory management systems to track all costs, including contractual costs, of maintaining and selling property. Inventory management systems should also generate management reports, provide controls and monitoring capabilities, and summarize information for the Office of Management and Budget and the Department of the Treasury. (See Treasury Report on Receivables).

B. Management of Guaranteed Loan Lenders and Servicers

REFERENCES

Guidance	Treasury/FMS "Managing Federal Receivables".
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1. *Lender Eligibility.* a. *Participation Criteria.* Federal credit granting agencies shall establish and publish in the **Federal Register** specific eligibility criteria for lender participation in Federally guaranteed loan programs. These criteria should include:

(1) Requirements that the lender is not currently debarred/suspended from participation in a Government contract or delinquent on a Government debt;

(2) Qualification requirements for principal officers and staff of the lender;

(3) Fidelity/surety bonding and/or errors and omissions insurance with the Federal Government as a loss payee, where appropriate, for new or non-regulated lenders or lenders with questionable performance under Federal guarantee programs;

(4) Financial and capital requirements for lenders not regulated by a Federal financial institution regulatory agency, including minimum net worth requirements based on business volume.

b. *Review of Eligibility.* Agencies shall review and document a lender's eligibility for continued participation in a guaranteed loan program at least every two years. Ideally, these reviews should be conducted in conjunction with on-site reviews of lender operations (see B.3) or other required reviews, such as renewal of a lender agreement (see B.2). Lenders not meeting standards for continued participation should be decertified. In addition to the participation criteria above, guarantor agencies should consider lender performance as a critical factor in determining continued eligibility for participation.

c. *Fees.* When authorized and appropriated for such purposes, agencies should assess non-refundable fees to defray the costs of determining and reviewing lender eligibility.

d. *Decertification.* Guarantor agencies should establish specific procedures to decertify lenders or take other appropriate action any time there is:

(1) Significant and/or continuing non-conformance with agency standards; and/or

(2) Failure to meet financial and capital requirements or other eligibility criteria.

Agency procedures should define the process and establish timetables by which decertified lenders can apply for reinstatement of eligibility for Federal guaranteed loan programs.

e. *Loan Servicers.* Lenders transferring and/or assigning the right to service guaranteed loans to a loan servicer should use only servicers meeting applicable standards set by the Federal guarantor agency. Where appropriate, agencies may adopt standards for loan servicers established by a Government Sponsored Enterprise (GSE) or a similar organization (e.g., Government National Mortgage Association for single family mortgages) and/or may authorize lenders to use servicers that have been approved by a GSE or similar organization.

2. *Lender Agreements.* Agencies should enter into written agreements with lenders that have been determined to be eligible for participation in a guaranteed loan program. These agreements should incorporate general participation requirements, performance standards and other applicable requirements of this Circular. Agencies are encouraged, where not prohibited by authorizing legislation, to set a fixed duration for the agreement to ensure a formal review of the lender eligibility for continued participation in the program.

a. *General Participation Requirements.*

(1) Requirements for lender eligibility, including participation criteria, eligibility

reviews, fees, and decertification (see *Section 1*, above);

(2) Agency and lender responsibilities for sharing the risk of loan defaults (see *Section II.3. a.(1)*); and, where feasible

(3) Maximum delinquency, default and claims rates for lenders, taking into account individual program characteristics.

b. *Performance Standards.* Agencies should include due diligence requirements for originating, servicing, and collecting loans in their lender agreements. This may be accomplished by referencing agency regulations or guidelines. Examples of due diligence standards include collection procedures for past due accounts, delinquent debtor counseling procedures and litigation to enforce loan contracts.

Agencies should ensure, through the claims review process, that lenders have met these standards prior to making a claim payment. Agencies should reduce claim amounts or reject claims for lender non-performance.

c. *Reporting Requirements.* Federal credit granting agencies should require certain data to monitor the health of their guaranteed loan portfolios, track and evaluate lender performance and satisfy OMB, Treasury, and other reporting requirements which include the Treasury Report on Receivables (TROR). Examples of these data which agencies must maintain include:

(1) *Activity Indicators*—number and amount of outstanding guaranteed loans at the beginning and end of the reporting period and the agency share of risk; number and amount of guaranteed loans made during the reporting period; and number and amount of guaranteed loans terminated during the period.

(2) *Status Indicators*—a schedule showing the number and amount of past due loans by

"age" of the delinquency, and the number and amount of loans in foreclosure or liquidation (when the lender is responsible for such activities).

Agencies may have several sources for such data, but some or all of the information may best be obtained from lenders and servicers. Lender agreements should require lenders to report necessary information on a quarterly basis (or other reporting period based on the level of lending and payment activity).

d. *Loan Servicers.* Lender agreements must specify that loan servicers must meet applicable participation requirements and performance standards. The agreement should also specify that servicers acquiring loans must provide any information necessary for the lender to comply with reporting requirements to the agency. Servicers may not resell the loans except to qualified servicers.

3. *Lender and Servicer Reviews.* To evaluate and enforce lender and servicer performance, agencies should conduct on-site reviews. Agencies should summarize reviews findings in written reports with recommended corrective actions and submit them to agency review boards. (See Section I.4.b.(1).)

Reviews should be conducted biennially where possible; however, agencies should conduct annual on-site reviews all lenders

and servicers with substantial loan volume or whose:

a. Financial performance measures indicate a deterioration in their guaranteed loan portfolio;

b. Portfolio has a high level of defaults for guaranteed loans less than one year old;

c. Overall default rates rise above acceptable levels; and/or

d. Poor performance results in collecting monetary penalties or an abnormally high number of reduced or rejected claims.

Agencies are encouraged to develop a lender/servicer classification system which assigns a risk rating based on the above factors. This risk rating can be used to establish priorities for on-site reviews and monitor the effectiveness of required corrective actions.

Reviews should be conducted by guarantor agency program compliance staff, Inspector General staff, and/or independent auditors. Where possible, agencies with similar programs should coordinate their reviews to minimize the burden on lenders/servicers and maximize use of scarce resources.

Agencies should also utilize the monitoring efforts of GSEs and similar organizations for guaranteed loans that have been "pooled".

4. *Corrective Actions.* If a review indicates that the lender/servicer is not in conformance with all program requirements, agencies should determine the seriousness of the problem. For minor non-compliance,

agencies and the lender or servicer should agree on corrective actions. However, agencies should establish penalties for more serious and frequent offenses. Penalties may include loss of guarantees, reprimands, probation, suspension, and decertification.

IV. Managing the Federal Government's Receivables

Agencies must service and collect debts, including defaulted guaranteed loans they have acquired, in a manner that best protects the value of the assets. Mechanisms must be in place to collect and record payments and provide accounting and management information for effective stewardship. Agencies should collect data on the status of their portfolios on a monthly basis although they are only required to report quarterly. These servicing activities can be carried out by the agency, or by third parties (such as private lenders or guaranty agencies), or a contract with a private sector firm. Unless otherwise exempt, the Debt Collection Improvement Act of 1996 (DCIA), codified at 31 U.S.C. 3711, requires Federal agencies to transfer any non-tax debt which is over 180 days delinquent to the Department of the Treasury/FMS for debt collection action (31 CFR Part 285). Under certain conditions, it may be advantageous to sell loans or other debts to avoid the necessity of debt servicing.

1. Accounting and Financial Reporting:

REFERENCES

Statutory	DCA, Chief Financial Officers Act (CFO) of 1990, Government Performance and Results Act, Federal Credit Reform Act of 1990, 31 U.S.C. 3719, 31 U.S.C. 3711, 2 U.S.C. 661.
Regulatory	31 CFR Part 285, OMB Circular No. A-127.
Guidance	JFMIP Standards on Direct and Guaranteed Loans, Instructions for the Treasury Report on Receivables Due from the Public (TROR), Treasury/FMS' "Managing Federal Receivables," Federal Accounting Standards Advisory Board—"Accounting for Direct Loans and Loan Guarantees," Statement of Federal Financial Accounting Standards No. 2, as amended," "Amendments to Accounting Standards for Direct Loans and Loan Guarantees," Statement of Federal Financial Accounting Standards No. 18.

a. *Accounting and Financial Reporting Systems.* Agencies shall establish accounting and financial reporting systems to meet the standards provided in this Circular, OMB Circular No. A-127, "Financial Management Systems", "JFMIP Standards on Direct and Guaranteed Loans", and other government-wide requirements. These systems shall be capable of accounting for obligations and outlays and of meeting the reporting requirements of OMB and Treasury, including those associated with the Federal Credit Reform Act of 1990 and the Chief Financial Officers (CFO) Act of 1990.

b. *Agency Reports.* Agencies should use comprehensive reports on the status of loan portfolios and receivables to evaluate

management effectiveness. Agencies shall prepare, in accordance with the CFO Act and OMB guidance, annual financial statements that include loan programs and other receivables. Agencies should also collect data for program performance measures (such as default rates, purchase rates, recovery rates, subsidy rates [actual vs. projected], and administrative costs) consistent with the Government Performance and Results Act of 1993 (GPRA) and Federal Credit Reform Act of 1990.

Agencies are also required to report periodically to Treasury on the status and condition of their non-tax delinquent portfolio on the TROR. Due to a timing difference between the submissions of fiscal

year-end data for the TROR, and data used for agency financial statements (the fiscal year-end receivables report is due in November and agency financial statements are not due until February/March of the following year), the data in these two reports may not be identical. Agencies should be able to explain differences and show the relationship of information contained in the two reports, but the reports are not required to reconcile.

2. *Loan Servicing Requirements.* Agency servicing requirements, whether performed in-house or by another agency or private sector firm, must meet the standards described below and in the Treasury/FMS publication Managing Federal Receivables.

REFERENCES

Statutory	Privacy Act of 1974, Debt Collection Act of 1982 (DCA), Debt Collection Improvement Act of 1996 (DCIA), 31 U.S.C. 3711.
Guidance	Treasury/FMS' "Managing Federal Receivables," and the "Guide to the Federal Credit Bureau Program".

a. *Documentation.* Approved loan files (or other systems of records) shall contain

adequate and up-to-date information reflecting terms and conditions of the loan,

payment history, including occurrences of delinquencies and defaults, and any

subsequent loan actions which result in payment deferrals, refinancing, or rescheduling.

b. *Billing and Collections.* Agencies shall ensure that there is routine invoicing of payments, and that efficient mechanisms are in place to collect and record payments. When making payments and where appropriate, borrowers should be encouraged to use agency systems established by Treasury which collect payments electronically, such as pre-authorized debits and credit cards.

c. *Escrow Accounts.* Agency servicing systems must process tax and insurance deposits for housing and other long-term real

estate loans through escrow accounts. Agencies should establish escrow accounts at the time of loan origination and payments for housing and other long-term real estate loans through an escrow account.

d. *Referring Account Information to Credit Reporting Agencies.* Agency servicing systems must be able to identify and refer debts to credit bureaus in accordance with the requirements of 31 U.S.C. 3711. Agencies shall refer *all* non-tax, non-tariff commercial accounts (current and delinquent) and *all* delinquent non-tariff and non-tax consumer accounts. Agencies may report *current* consumer debts as well and are encouraged to do so. The reporting of current data (in

addition to any delinquencies) provides a truer picture of indebtedness while simultaneously reflecting accounts that the borrower has maintained in good standing. There is no minimum dollar threshold, *i.e.*, accounts (debts) owed for as low as \$5 may be referred to credit reporting agencies. Agencies shall require lenders participating in Federal loan programs to provide information relating to the extension of credit to consumer or commercial credit reporting agencies, as appropriate. For additional information, agencies should refer to Treasury/FMS' Guide to the Federal Credit Bureau Program.

3. *Asset Resolution*

REFERENCES

Statutory	DCIA, 31 U.S.C. 3711(i); Federal Credit Reform Act of 1990, 2 U.S.C. 661.
Guidance	OMB Circular No. A-11, Section 85.7, OMB Circular No. A-34.

a. The DCIA, as codified at 31 U.S.C. 3711(i) authorizes agencies to sell any non-tax debt owed to the United States that is more than 90 days delinquent, subject to the provisions of the Federal Credit Reform Act of 1990. The Administration's budget policy is that agencies are required to sell any non-tax debts that are delinquent for more than one year for which collection action has been terminated, if the Secretary of the Treasury determines that the sale is in the best interest of the United States Government. Agencies are required to sell the debts for cash or a combination of cash and profit participation, if such an arrangement is more advantageous to the government, and make the sales without recourse. Loan sales should result in shifting agency staff resources from servicing to mission critical functions.

Beginning in FY 2000, for programs with \$100 million in assets (unpaid principal balance) that are delinquent for more than two years, the agency is expected to dispose of assets expeditiously. (See OMB Circular No. A-11.) Agencies may request from OMB, an exception for the following:

- (1) Loans to foreign countries and entities;
- (2) Loans in structured forbearance, when conversion to repayment status is expected within 24 months or after statutory requirements are met;
- (3) Loans that are written off as unenforceable *e.g.*, due to death, disability, or bankruptcy;
- (4) Loans that have been submitted to Treasury for offset and are expected to be extinguished within three (3) years;
- (5) Loans in adjudication or foreclosure; and
- (6) Student loans.

Agencies shall provide to OMB an annual list of loans that are exempted.

b. *Evaluate Asset Portfolio.* On an annual basis, agencies shall take steps to evaluate and analyze existing asset portfolios and

programs associated therewith, to determine if there are avenues to:

(1) *Improve Credit Management and Recoveries.* Improvement in current management, performance, and recoveries of asset portfolios shall be reviewed against current marketplace practices;

(2) *Realize Administrative Savings.* Analyses of current asset portfolio practices shall include the benefit of transferring all or some portion of the portfolio to the private sector. Agencies shall develop a staffing utilization plan to ensure that when asset sales result in a decreased workload, staff are shifted to priority workload mission critical functions.

(3) *Initiate Prepayment.* Agencies shall initiate prepayment programs when statutorily mandated or, if upon analysis of an existing asset portfolio practice, it is deemed appropriate. Prepayment programs may be initiated without the approval of OMB. Delinquent borrowers may participate in a prepayment program only if past due principal, interest, and charges are paid in full prior to their request to prepay the balance owed.

c. *Financial Asset Services.* Agencies shall engage the services of outside contractors as deemed necessary to assist in its asset resolution program. Contractors providing various types of asset services are available through the General Services Administration's Multiple Award Schedule for Financial Asset Services as follows:

- (1) Program Financial Advisors;
- (2) Transaction Specialists
- (3) Due Diligence Contractors;
- (4) Loan Service/Asset Managers; and
- (5) Equity Monitors/Transaction Assistants.

d. *Loan Asset Sales Guidelines.* OMB and Treasury jointly will update existing guidelines and procedures to implement loan prepayment and loan asset sales. In accordance with the agreed upon procedures,

agencies conducting such prepayment and loan asset sales programs will consult with both OMB and Treasury throughout the prepayment and loan asset sales processes to ensure consistency with the agreed upon policies and guidelines. Unless an agency can document from their past experience that the sale of certain types of loan assets is not economically viable, a financial advisor shall be engaged by each agency to conduct a portfolio valuation and to compare pricing options for a proposed prepayment plan or loan asset sale. Based on the financial advisor's report, the agencies will develop a prepayment or loan asset sales schedule and plan, including an analysis of the pricing option selected. As part of the ongoing consultation between OMB, Treasury, and the agencies, prior to proceeding with their prepayment or loan asset sales, the agencies will submit their final prepayment or loan asset sales plans and proposed pricing options to OMB and Treasury for review in order to ensure that any undue cost to the Government or additional subsidy to the borrower is avoided. The agency Chief Financial Officer will certify that an agency loan prepayment and loan asset sales program is in compliance with the agreed upon guidelines. See Asset Sales Guidelines.

V. *Delinquent Debt Collection*

Agencies shall have a fair but aggressive program to recover delinquent debt, including defaulted guaranteed loans acquired by the Federal Government. Each agency will establish a collection strategy consistent with its statutory authority that seeks to return the debtor to a current payment status or, failing that, maximize collection on the debt.

1. *Standards for Defining Delinquent and Defaulted Debt*

REFERENCES

Statutory	DCA/DCIA/31 U.S.C. 3701, 3711-3720D.
Regulatory	Federal Claims Collection Standards, 31 CFR 900.2(b).
Guidance	Treasury/FMS' "Managing Federal Receivables".

The Federal Claims Collections Standards define delinquent debt in general terms. Agency regulations may further define delinquency to meet specific types of debt or program requirements.

a. *Direct Loans.* Agencies shall consider a direct loan account to be delinquent if a payment has not been made by the date specified in the agreement or instrument (including a post-delinquency payment agreement), unless other satisfactory payment arrangements have been made.

b. *Guaranteed Loans.* Loans guaranteed or insured by the Federal Government are in default when the borrower breaches the loan agreement with the private sector lender. A default to the Federal Government occurs when the Federal credit granting agency repurchases the loan, pays a loss claim or pays reinsurance on the loan. Prior to establishing a receivable on the agency financial records, each agency must consider statutory and regulatory authority applicable to the debt in order to determine if the

agency has a legal right to subject the debt to the collection provisions of this Circular.

c. *Other Debt.* Overpayments to contractors, grantees, employees, and beneficiaries; fines; fees; penalties; and other debts are delinquent when the debtor does not pay or resolve the debt by the date specified in the agency's initial written demand for payment (which generally should be within 30 days from the date the agency mailed notification of the debt to the debtor).

2. Administrative Collection of Debts

REFERENCES

Statutory	15 U.S.C. 1673(a)(2), 31 U.S.C. 3701, 3711–3720E, 26 U.S.C. 6402, 5 U.S.C. 5514, Fair Debt Collection Practices Act.
Regulatory	31 CFR Part 285, Federal Claims Collection Standards, 31 CFR Part 901, Federal Claims Collections Standards, 5 CFR part 550, subpart K, 26 CFR 301.6402–1 through 301.6402–7, Federal Acquisitions Regulations, Subpart 32.6.
Guidance	Treasury/FMS "Managing Federal Receivables" and FMS Cross-servicing/Offset Guidance Documents, Treasury's/FMS' "Guide to the Federal Credit Bureau Program".

Agencies shall promptly act on the collection of delinquent debts, using all available collection tools to maximize collections. Agencies shall transfer debts delinquent 180 days or more to the Treasury/FMS or Treasury-designated debt collection centers for further collection actions and resolution. Exceptions to this requirement (e.g., the debt has been referred for litigation) can be found in 31 U.S.C. 3711 and 31 CFR 285.12(d).

a. *Collection Strategy.* Agencies shall maintain an accurate and timely reporting system to identify and monitor delinquent receivables. Each agency shall develop a systematic process for the collection of delinquent accounts. Collection strategies shall take full advantage of available collection tools while recognizing program needs and statutory authority.

b. *Collection Tools for Debts Less than 180 Days Delinquent.* Agencies may use the following collection tools when the debt is fewer than 180 days delinquent:

(i) *Demand Letters.* As soon as an account becomes delinquent, agencies should send demand letters to the debtor. The demand letter must give the debtor notice of each form of collection action and type of financial penalty the agency plans to use. Additional demand letters may be sent if necessary. See 31 U.S.C. 3711, 31 CFR Part 285 and 901.2.

For consumer accounts, the first demand letter or initial billing notice should include the 60 day notification requirement of the agency's intent to refer to a credit bureau. Once the 60 day period has passed, the agency should initiate reporting if the account has not been resolved. This will also enable uninterrupted reporting to credit bureaus by cross-servicing agencies. The 60 day notification of intent to refer to a credit bureau is not required for commercial accounts. (See Treasury/FMS' Guide to the Federal Credit Bureau Program.)

(ii) *Internal Offset.* If the agency that is owed the debt also makes payments to the debtor, the agency may use internal offset to the extent permitted by that agency's statutes and regulations and the common law. Delinquent debts owed by an agency's

employees may be offset in accordance with statutes and regulations administered by the Office of Personnel Management. See OPM regulations and statutes.

(iii) *Treasury Offset Program.* Agencies may collect delinquent debt, which is less than 180 days delinquent, by referring those debts to Treasury/FMS in order to offset Federal payments due to the debtor. Payments, which Treasury will offset, include certain benefit payments, federal retirement payments, salaries, vendor payments and tax refunds. 31 U.S.C. 3716, 31 U.S.C. 3720A, 31 CFR Part 285, 26 CFR 301.6402, 31 CFR Chapter II, 901.3, and, Federal Acquisition Regulations Subpart 32.6. If a Federal payment has not yet been initiated in the Treasury Offset Program, agencies may request that the paying agency perform the offset.

(iv) *Administrative Wage Garnishment.* Agencies have the authority to administratively garnish the wages of delinquent debtors in order to recover delinquent debt. The maximum garnishment for any one debt is 15% of disposable pay. Multiple garnishments from all sources against one debtor's wages may not exceed 25% of disposable pay of an individual. 31 U.S.C. 3720D, 31 CFR 285.11 and 15 U.S.C. 1673(a)(2).

(v) *Contracting with Private Collection Agencies.* Treasury has contracted with private collection agencies that may be used by Federal agencies to provide assistance in the recovery of delinquent debt owed to the Government. 31 U.S.C. 3711, 31 U.S.C. 3718, 31 CFR Parts 285, and 901, Fair Debt Collection Practices Act. Agencies may also transfer debts to Treasury prior to 180 days for the purpose of referral to private collection agencies.

(vi) *Treasury Cross-Servicing.* Agencies may transfer debts to Treasury for full servicing at any time after the due process requirements. (See 31 CFR Part 285.)

c. *Collection of Debts Which are Over 180 Days Delinquent.* This paragraph sets forth Treasury's collection procedures for debts which are over 180 days delinquent.

(i) *Treasury Offset Program.* The DCIA requires that all agencies recover debt

delinquent more than 180 days by referring those debts to the Treasury for offset of tax refunds and other Federal payments.

Agencies must refer all accounts for offset in accordance with guidance provided by the Department of the Treasury/FMS. Federal Claims Collection Standards, 31 U.S.C. 3716, 31 U.S.C. 3720A and 31 CFR Part 285. The following types of offset are undertaken in the Treasury Offset Program (TOP):

- (1) Tax Refund Offset;
- (2) Vendor Offset;
- (3) Federal Retirement Offset;
- (4) Salary Offset;
- (5) Benefit Offset (At the time of publication, benefit payments have not been incorporated into the program. Benefit payments, such as Social Security Administration (SSA), Black Lung and Railroad Retirement Benefits (RRB) will be added in the future.); and
- (6) Other Federal payments as allowed by law (as such payments are allowed into the program).

(ii) *Cross-Servicing.* The DCIA requires that all debts owed to agencies which are more than 180 days delinquent shall be transferred to Treasury/FMS or a Treasury-designated debt collection center for servicing. The DCIA contains provisions and requirements for exempting certain classes of debts from being transferred for servicing www.treas.fms.gov/debt. (See 31 U.S.C. 3711, and 31 CFR Part 285.) Once debts are transferred to Treasury, agencies must cease all collection activities other than maintaining accounts for the Treasury Offset Program.

Once Treasury has received a debt for servicing, the appropriate debt collection actions will be taken. These actions may include sending demand letters; phone calls to delinquent debtors; credit bureau reporting; referring debtors to the Treasury Offset Program; referring debtors to private collection agencies; administrative wage garnishment; and any other available debt collection tool.

3. Referrals to the Department of Justice

A. Referral for Litigation

REFERENCES

Statutory	31 U.S.C. 3711, 28 U.S.C. 3001, 3002(1).
Regulatory	31 CFR Part 904, Federal Claims Collection Standards.
Guidance	Department of the Treasury/FMS "Litigation Referral Process Handbook," and "Managing Federal Receivables," Appendix 8.

Agencies, including Treasury/FMS or Treasury-designated debt collection centers, shall refer delinquent accounts to the Department of Justice, or use other litigation authority that may be available, as soon as there is sufficient reason to conclude that full or partial recovery of the debt can best be achieved through litigation. Referrals to Justice should be made in accordance with the Federal Claims Collection Standards. If the debtor does not come forward with a voluntary payment after the claim has been referred for litigation, a lawsuit shall be initiated promptly.

1. In consultation with the Department of Justice, agencies shall establish a system to account for: (a) Claims referred to Justice, and (b) claims closed by Justice and returned to the respective agencies.
 2. Agencies shall accelerate claim referrals to the Department of Justice in those districts where the Department of Justice contracts with private law firms for debt collection.
 3. Agencies shall stop the use of any collection activities including TOP and refrain from further contact with the debtor once a claim has been referred to the Department of Justice, unless the Department

of Justice agrees to allow the debtor(s) to remain in TOP for offset while they pursue other legal remedies.

4. Agencies shall promptly notify the Department of Justice of any payments received on a debtor's account after referral of the claim for litigation.

5. The Department of Justice shall account to agencies for monies or property collected on claims referred by the agencies.

B. Referral for Approval of Compromise Offer

REFERENCES

Statutory	31 U.S.C. 3711.
Regulatory	31 CFR Part 902, Federal Claims Collection Standards.
Guidance	Treasury/FMS' "Managing Federal Receivables".

Agencies may compromise a debt within their jurisdiction when the principal balance of the debt is less than \$100,000 (or any higher amount authorized by the U.S. Attorney General). Unless otherwise

provided by law, when the principal balance of the debt is greater than \$100,000 (or any higher amount authorized by the U.S. Attorney General), the compromise authority

rests with the Department of Justice. 31 CFR Part 902.

C. Referral for Approval to Terminate Collection Activity

REFERENCES

Statutory	31 U.S.C. 3711.
Regulatory	31 CFR Part 902, Federal Claims Collection Standards.
Guidance	Treasury/FMS' "Managing Federal Receivables".

Agencies may terminate collection on a debt within their jurisdiction when the principal balance of the debt is less than \$100,000 (or any higher amount authorized by the U.S. Attorney General). Unless

otherwise provided by law, when the principal balance of the debt is greater than \$100,000 (or any higher amount authorized by the U.S. Attorney General), the authority

to terminate rests with the Department of Justice. (See 31 CFR Part 902.)

4. Interest, Penalties and Administrative Costs

REFERENCES

Statutory	31 U.S.C. 3717.
Regulatory	Federal Claims Collection Standards, 31 CFR 901.9.
Guidance	Treasury's "Managing Federal Receivables," Chapter 4.

Interest, penalties and administrative costs should be added to all debts unless a specific statute, regulation, loan agreement, contract, or court order prohibits such charges or sets criteria for their assessment. Agencies shall assess late payment interest on delinquent debts. Further, agencies shall assess a penalty charge of not more than six percent (6%) per year for failure to pay a debt more than ninety (90) days past due, unless a statute,

regulation required by statute, loan agreement, or contract prohibits charging interest or assessing charges or explicitly fixes the interest rate or charges. (See 31 U.S.C. 3717 (e) and (g)). A debt is delinquent when the scheduled payment is not paid in full by the payment due date contained in the initial demand letter or by the date specified in the applicable agreement or instrument. Agencies shall assess administrative costs to

cover the cost of processing and handling delinquent debt. Agencies must adjust the interest rate on delinquent debt to conform with the rate established by a U.S. Court when a judgment has been obtained.

5. Termination of Collection, Write-Off, Use of Currently Not Collectible (CNC), and Close-Out

REFERENCES

Statutory	31 U.S.C. 3711; 26 CFR 1.6050P-0, 26 CFR 1.6050P-1.
Regulatory	31 CFR Part 903 Federal Claims Collection Standards, 26 CFR 1.6050P-1.
Guidance	FCPWG Final Report on Write-off Policy, Dated 12/15/98, Treasury/FMS "Managing Federal Receivables".

All debt must be adequately reserved for in the allowance account. All write-offs must be made through the allowance account. Under no circumstances are debts to be written off directly to expense. Generally, write-off is mandatory for delinquent debt older than two years unless documented and justified to OMB in consultation with Treasury. Once the debt is written-off, the agency must either classify the debt as currently not collectible (CNC) or close-out the debt. Cost effective collection efforts should continue, specifically, if an agency determines that continued collection efforts after mandatory write-off are likely to yield higher returns. In such cases the written-off debt is not closed out but classified as CNC. The collection process continues until the agency determines it is no longer cost effective to pursue collection. At that point, the debt should be closed-out.

Under no circumstances should internal controls be compromised by the write-off or reclassification of debt. Very small percentages of debt older than two years can

frequently result in amounts that, while immaterial to the overall debt and write-off balances, are large enough to pose a risk of fraud and abuse. If collection efforts are ongoing then adequate internal controls must be maintained.

In those cases where material collections can be documented to occur after two years, debt cannot be written off until the estimated collections become immaterial.

During the period debts are classified as CNC, agencies should maintain the debt for administrative offset and other collection tools, as described in the FCCS until: (1) The debt is paid; (2) the debt is closed out; or (3) all collection actions are legally precluded; or (4) the debt is sold, whichever occurs first. When an agency closes out a debt, the agency must file a Form 1099C with the Internal Revenue Service (IRS) and notify the debtor in accordance with the Internal Revenue Code 26 U.S.C. 6050P and IRS regulations 26 CFR 1.6050P-1. The 1099C reports the uncollectible debt as income to the debtor which may be taxable at the debtor's current

tax rate. Reporting the discharge of indebtedness to the IRS results in a potential benefit to the Federal Government, because any payments made to the IRS augment government receipts. Agencies should report closed-out debts on the Treasury Report on Receivables Due from the Public (TROR). Agencies must stop all collection activity, including the sale of debts, once debts are closed out. Agencies must not close out debts which have been sold or are scheduled to be sold.

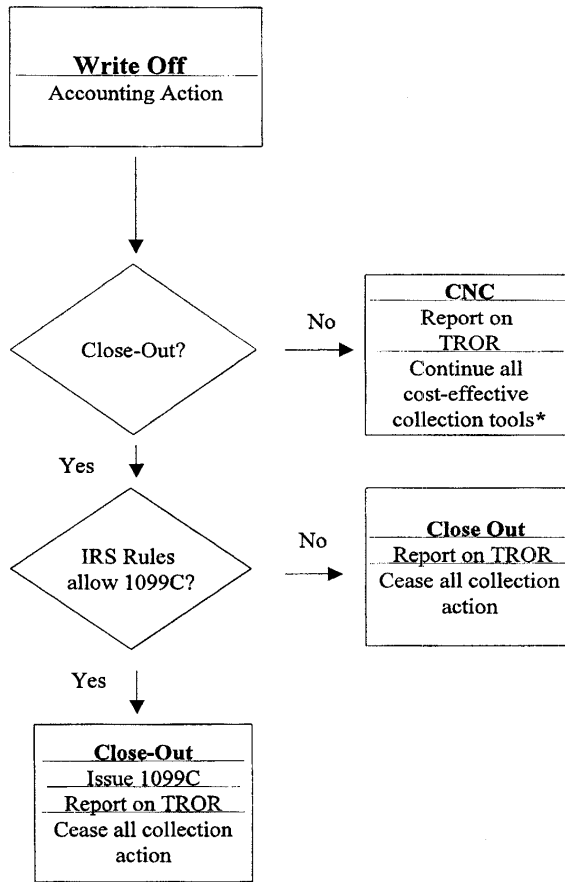
Note: "Termination" and "suspension of collection" are legal procedures, which are separate and distinct from the accounting procedure of "write-off." Agencies shall consult the Federal Claims Collection Standards, Part 903 for requirements which must be met prior to terminating or suspending collection. (See the attached Write-off/Close-out Process Flowchart for Receivables.)

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APPENDIX A to CIRCULAR NO. A-129

ATTACHMENT

Write-off occurs when the agency determines that the likelihood of collection is less than 50%, but no later than two years from the date of delinquency.



* Debt collection tools are described in Appendix A, Section V of this Circular. Agencies should use all tools, as appropriate, prior to and after the debt is written off.

Appendix B to OMB Circular A-129**Checklist for Credit Program Legislation, Testimony, and Budget Submissions**

The following checklist provides guidelines to be followed in reviewing credit program legislation, testimony, and budget submissions.

The checklist is to be used by agencies and OMB in proposing legislation, reviewing credit proposals, and preparing testimony on credit activities. If the proposed provisions or language are not in conformity with the policies of this Circular as listed in these checklists, agencies will be required to request in writing that the Office of Management and Budget modify or waive the requirement. Waiver request forms are available from OMB for this purpose. Such requests will identify the modification(s) or waiver(s) requested, and also will state the reasons for the request and the time period for which the exception is required. Exceptions, when allowed, will ordinarily be granted only for a limited time, in order to allow for continuing review by OMB.

Agencies are to use the checklist in the budget submission process for the evaluation of existing legislation, regulations, or program policies. The OMB program examiner with primary responsibility for the credit account will determine the use of this checklist. Use of the list includes review of changes in financial markets and the status of borrowers and beneficiaries to ensure that Federal objectives require continuation of the credit program. If these policies are found to be not in conformity with the policies of this Circular, agencies will propose changes to correct the inconsistency in their annual budget submission and justification to OMB and the Congress. When an agency does not deem a change in existing legislation, regulations, or policies to be desirable, it will provide a justification for retaining the existing non-conforming legislation or policies in its budget submission to OMB at the request of the budget examiner.

Checklist—Federal credit program justification should include the following elements:

1. Program title;
2. Form of Assistance (direct or guarantee);
3. Federal objectives of this program: (II.1.a.);
4. Reasons why Federal credit assistance is the best means to achieve these objectives: (II.1.a.);
5. Any draft bill establishing a credit program should contain the following:
 - Authorization to extend direct loans or make loan guarantees subject to the requirements of the Federal Credit Reform Act of 1990, as amended.
 - Authorization and requirement for a subsidy appropriation.
 - Cap on volume of obligations or commitments. (II.3.e.)
 - Terms and conditions defined sufficiently and precisely enough to estimate subsidy rate. (State estimated subsidy of this program (rate and dollar amount).) (II.1.e.)
 - Authorization of administrative expenses.

6. Describe briefly the existing and potential private sources of credit (and type of institution): (II.1.a.(2)(a)).

7. Explain reasons why private sources of financing and their terms and conditions must be supplemented and subsidized, including:

- To correct a defined capital market imperfection;
- To subsidize identified borrowers or other beneficiaries; and/or
- To encourage certain specified activities. (II.1.a.(1)).

8. State reasons why a federal credit subsidy is the most efficient way of providing assistance, how it provides assistance in overcoming market imperfections, and how it assists the identified borrowers or beneficiaries or encourages the identified activities. (II.1.b.).

9. Summarize briefly the benefits expected from the program. Can the value of these benefits (or some of these benefits) be estimated in dollar terms? If so, state the estimate of their value. Further information on conducting cost-benefit analysis can be found in OMB Circular No. A-94. (II.1.c.).

10. Describe any elements of program design which encourage and supplement private lending activity, such that private lending is displaced to the smallest degree possible by agency programs. (II.1.d.).

11. Estimate the expected administrative (including origination, servicing, and collection) resource requirements and costs of the credit program (dollar amounts over next 5 fiscal years). (II.1.f.).

12. Prohibitions: (II.2.c.&d.).

Agencies will not guarantee federally tax-exempt obligations directly or indirectly. Agencies will not subordinate direct loans to tax-exempt obligations and will provide that effective subordination of guaranteed loans to tax-exempt obligations will render the guarantee void. Risk sharing: (II.3.a.).

- Lenders and borrowers share a substantial stake in full repayment according to the loan contract.
- Private lenders who extend Government guaranteed credit bear at least 20 percent of any potential losses.
- Borrowers deemed to pose less of a risk receive a lower guarantee as a percentage of the total loan amount.
- Borrowers have an equity interest in any asset being financed by the credit assistance. Fees and interest rates: (II.3.b).
- Interest and fees are set at levels that minimize default and other subsidy costs.
- Interest rates charged to borrowers (or interest supplements) not set at an absolute level, but instead set by reference to the rate (yield) on benchmark Treasury.
- Protecting the Government's interest:
 - Contractual agreements include all covenants and restrictions (e.g., liability insurance) necessary to protect the Federal Government's interest. (II.3.c.).
 - Maturities on loans shorter than the estimated useful economic life of any assets financed. (II.3.c.(1)).
 - The Government's claims on assets not subordinated to the claim of other lenders in the case of a borrower's default. (II.3.c.(2)).

- Loan contracts to be standardized and private sector documents used to the extent possible. (II.3.f.).

13. Describe the methods used to evaluate the program and the results of evaluations that have been made. (II.4.c.(1)).

Appendix C to OMB Circular A-129**Model Bill Language for Credit Programs****A Bill**

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

That, this Act may be cited as " ".

Authorization

Sec. 2.(a) The Administrator is authorized to make or guarantee loans to * * * (Define eligible applicants).

(b) There are authorized to be appropriated \$ for the cost of direct loans or loan guarantees authorized in subsection (1) and \$ for administrative expenses for fiscal year and such sums as shall be necessary for each fiscal year thereafter. [The amounts authorized must be consistent with the amounts proposed in the President's budget for that fiscal year. Generally, a specific amount should be specified for the first fiscal year and sums for subsequent fiscal years (see OMB Circular No. A-19.)]

Within the resources and authority available, gross obligations for the principal amount of direct loans offered by the Administrator will not exceed \$, or the amount specified in appropriations acts for fiscal year and such sums as shall be necessary for each fiscal year thereafter. Commitments to guarantee loans may be made by the Administrator only to the extent that the total loan principal, any part of which is guaranteed, will not exceed \$, or the amount specified in appropriations acts for fiscal year and such sums as shall be necessary for each fiscal year thereafter.

Terms and Conditions

Sec. 3. Loans made or guaranteed under this Act will be on such terms and conditions as the Administrator may prescribe, except that:

(a) The Administrator will allow credit to any prospective borrower only when it is necessary to alleviate a credit market imperfection, or when it is necessary to achieve specified Federal objectives by providing a credit subsidy and a credit subsidy is the most efficient way to meet those objectives on a borrower-by-borrower basis.

(b) The final maturity of loans made or guaranteed within a period shall not exceed years, or percent of the useful life of any physical asset to be financed by the loan, whichever is less as determined by the Administrator.

(c) No loan guaranteed to any one borrower will exceed 80% of the loss on the loan. Borrowers who are deemed to pose less of a risk will receive a lower guarantee as a percentage of the loan amount.

(d) No loan made or guaranteed will be subordinated to another debt contracted by the borrower or to any other claims against the borrowers in the case of default.

(e) No loan will be guaranteed unless the Administrator determines that the lender is responsible and that adequate provision is made for servicing the loan on reasonable terms and protecting the financial interest of the United States.

(f) No loan will be guaranteed if the income from such loan is excluded from gross income for the purposes of Chapter 1 of the Internal Revenue Code of 1986, as amended, or if the guarantee provides significant collateral or security, as determined by the Administrator, for other obligations the income from which is so excluded.

(g) Direct loans and interest supplements on guaranteed loans will be at an interest rate that is set by reference to a benchmark interest rate (yield) on marketable Treasury securities with a similar maturity to the direct loans being made or the non-Federal loans being guaranteed. The minimum interest rate of these loans will be (at) (percent above) (no more than percent below) the interest rate of the benchmark financial instrument.

(h) The minimum interest rate of new loans will be adjusted every quarter (month(s)) (weeks) (days) to take account of changes in the interest rate of the benchmark financial instrument. (see

(i) Fees or premiums for loan guarantee or insurance coverage will be set at levels that minimize the cost to the Government (as defined in Section 502 of the Federal Credit Reform Act of 1990, as amended) of such coverage, while supporting achievement of the program's objectives. The minimum guarantee fee or insurance premium will be

(at) (no more than percent below) the level sufficient to cover the agency's costs for paying all of the estimated costs to the Government of the expected default claims and other obligations. Loan guarantee fees will be reviewed every month(s) to ensure that the fees assessed on new loan guarantees are at a level sufficient to cover the referenced percentage of the agency's most recent estimates of its costs.

(j) Any guarantee will be conclusive evidence that said guarantee has been properly obtained; that the underlying loan qualified for such guarantee; and that, but for fraud or material misrepresentation by the holder, such guarantee will be presumed to be valid, legal, and enforceable.

(k) The Administrator will prescribe explicit standards for use in periodically assessing the credit risk of new and existing direct loans or guaranteed loans. The Administrator must find that there is a reasonable assurance of repayment before extending credit assistance.

(l) New direct loans may not be obligated and new loan guarantees may not be committed except to the extent that appropriations of budget authority to cover their costs are made in advance, as required in Section 504 of the Federal Credit Reform Act of 1990, as amended.

Payment of Losses

Sec. 4(a). If, as a result of a default by a borrower under a guaranteed loan, after the holder thereof has made such further collection efforts and instituted such enforcement proceedings as the

Administrator may require, the Administrator determines that the holder has suffered a loss, the Administrator will pay to such holder percent of such loss, as specified in the guarantee contract. Upon making any such payment, the Administrator will be subrogated to all the rights of the recipient of the payment. The Administrator will be entitled to recover from the borrower the amount of any payments made pursuant to any guarantee entered into under this Act.

(b) The Attorney General will take such action as may be appropriate to enforce any right accruing to the United States as a result of the issuance of any guarantee under this Act.

(c) Nothing in this section will be construed to preclude any forbearance for the benefit of the borrower which may be agreed upon by the parties to the guaranteed loan and approved by the Administrator, provided that budget authority for any resulting subsidy costs as defined under the Federal Credit Reform Act of 1990, as amended, is available.

(d) Notwithstanding any other provision of law relating to the acquisition, handling, or disposal of property by the United States, the Administrator will have the right in his discretion to complete, recondition, reconstruct, renovate, repair, maintain, operate, or sell any property acquired by him pursuant to the provisions of this Act.

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APPENDIX IV

**Suggested Responses
To
Discussion Examples**

Suggested Responses to Discussion Examples

Section B—DEFINITIONS and Rules

Example A

Most of the residential loans in Nickelville and the surrounding area are made by Central Bank; the rest are made by two small commercial banks. The only state certified residential appraiser in town does all of Central's appraisals in and around Nickelville, and this is a substantial part of her work. There are several licensed real estate brokers who render market value opinions as a secondary business.

Recently, new management has taken over Central, and the institution has become much more aggressive in making loans. Loan officers now operate on a commission basis and actively seek new loans.

In recent weeks several appraisals have come in below the proposed sale prices. Each time this happens, the loan officer calls the appraiser in to "discuss" the appraisal. The loan officers and the selling brokers are pressuring her to "go along" with the deal. In one case, there was only a few hundred dollars difference on a \$90,000 value, but in several others the proposed sale prices were at the extreme top end of the value ranges indicated by the comparables. In one case, the proposed price was outside the range entirely. The appraiser tries to use the best, most recent comparables and feels that she does careful, objective appraisals. She sincerely wants to be of service to her clients and is concerned; in this case, she is not doing so. What latitude within USPAP does the appraiser have?

Response

The question is, should "pleasing" the client enter into the appraiser's thinking at all?

Appraisal is a service profession, but the way to serve clients is to insist (for their own good) that they allow you to work independently. Appraisers should not be pressured into making underwriting decisions that should be made by the lender. The **Conduct** section of the **ETHICS RULE** clearly requires that appraisers provide their services in an independent, impartial, and unbiased manner. To do less is a disservice to those who rely on the integrity of the lending system, which protects depositors, bondholders, and, ultimately, taxpayers. It is not possible to be objective or unbiased without appraiser independence.

Example B

A certified general appraiser prepared an appraisal report of a motel in May 1997, and testified about the appraisal in court in June 1998. The trial court issued its decision in July 1998. The decision was appealed, and in December 1998, the appellate court remanded the case to the trial court for further consideration. The trial court considered the case in July 2000, and that decision was appealed. The appeal is still pending. How long should the appraiser keep his workfile?

Response

In analyzing this case, refer to the **Record Keeping** section of the **ETHICS RULE**. The five-year period after the date the appraisal report was prepared expired five years after May 1997 (or May 2002), but the appraiser is required to keep the workfile for at least two years after the final disposition of the case, whenever that occurs.

Under USPAP, appraisers must measure both the five-year period following preparation of the report and the two-year period following final disposition of the case. The workfile must be retained until both periods expire.

Example C

A fee appraiser is trying to get on the approved list for a local mortgage company. To be considered for approval, the lender requires an appraiser to provide “sample” appraisal reports performed within the past year. The lender also requires each appraiser to pay a fee to be included on the lender’s approved appraiser list. Is there a way the appraiser can provide the sample appraisal reports under USPAP? Also, is it ethical for the appraiser to pay a fee to the lender?

Response

The answer to the first question is yes. In order to provide this information an appraiser must satisfy the **Confidentiality** section of the **ETHICS RULE**. The confidential nature of the client-appraiser relationship must be protected. The appraiser in this case has three options:

1. Turn down the request to provide the information, or
2. Secure a release from the client for each appraisal report, or
3. Provide sample reports, but redact all information that should not be provided to anyone other than the client, such as confidential information or assignment results.

For the second question, the answer is also yes. It is ethical for an appraiser to pay a fee to be included on the lender’s approved list provided the appraiser discloses payment of a fee in the appraisal reports. The **Management** section of the **ETHICS RULE** addresses this issue and provides guidance. It states that disclosure of fees connected to the procurement of an assignment **must appear in the certification and in any transmittal letter in which conclusions are stated** (bold added for emphasis).

Example D

An appraiser has been asked by Global Relocation Corporation to appraise the home of a transferring employee. The owners are at home when the appraiser arrives to inspect the house. They follow him around, pointing out features of the house as he makes his inspection. As the appraiser prepares to leave, the owner asks, “Well, what’s it worth?” The appraiser patiently explains the appraisal process, pointing out that this is only the first step and much work needs to be done before he will have an opinion of the house’s value. The next day he is finishing the appraisal when the telephone rings. It’s the owner and he wants to know the value opinion. The appraiser tells him the value conclusion and is careful to fulfill the requirements for an oral report as stated in **STANDARD 2** of the *Uniform Standards of Professional Appraisal Practice*. Has the appraiser conducted himself properly?

Response

This example illustrates how the **Confidentiality** section of the **ETHICS RULE** can be violated. This section states that:

*an appraiser must not disclose confidential information or **assignment results** prepared for a client to anyone other than the client and persons specifically authorized by the client; state enforcement agencies and such third parties as may be authorized by due process of law; and a duly authorized professional peer review committee except when such disclosure to a committee would violate applicable law or regulation. (Bold added for emphasis.)*

The appraiser's value conclusion is an assignment result and the **Confidentiality** section of the **ETHICS RULE** governs the release of this information. In this case, the client is the relocation company. Disclosing the assignment results to the property owner without the permission of the relocation company is a violation of the **Confidentiality** section of the **ETHICS RULE**.

Example E

Two months ago an appraiser appraised a property for a lender. The sale, which was pending at the time of the appraisal, ultimately fell through and the loan was never made. The appraiser has just been asked by another lender to appraise the property for financing in connection with a new purchase agreement. The appraiser is wondering whether or not he can accept this assignment. Under what conditions **might** he accept this assignment? Is it acceptable for him simply to change the client's name on the report?

Response

Is it acceptable for the appraiser to reappraise this property? It depends on the circumstances. The concerns here are confidentiality, the appraiser-client relationship, and identification of the client and intended users.

The key determinant in deciding whether or not one can reappraise the same property for another client is the presence of confidential information. The **Confidentiality** section of the **ETHICS RULE** is relevant. Accepting the assignment from the second potential client is not prohibited by USPAP, assuming any existing confidential information is handled properly.

An appraiser cannot disclose the results of a specific assignment to anyone other than the client and those designated by the client. The definitions of the terms *assignment*, *client*, and *assignment results* are helpful to this situation and should be reviewed. As stated in the **DEFINITIONS** section of USPAP, both the client and the assignment results are specific to an assignment. Therefore, valuation services performed for a new client would constitute a new assignment and the assignment results would be specific to that new assignment.

If the prior assignment included any confidential information, its disclosure to a different client or intended user would violate the **ETHICS RULE** if the information were still classified as confidential. This includes the requirement to comply with all confidentiality and privacy laws and regulations. The appraiser may, however, accept the second assignment, making sure not to disclose any confidential information from the original assignment to the second client, if the original client grants permission for its disclosure and use; the information is available from another source; or, if the confidential information is not material to deriving credible assignment

results based on the second assignment's intended use. If any one of the three circumstances does not exist, then the second potential assignment must be declined.

If the appraiser determines that the second assignment can be taken, the appraiser must treat this as a new assignment. This will require the appraiser to determine the appropriate scope of work necessary to complete this new assignment (**Standards Rule 1-2(f)**) and disclose that scope of work in the report (**Standards Rules 2-2 (a), (b), and (c)(vii)**).

Is it acceptable for the appraiser to simply change the client name on the report?

No. The **Conduct** section of the **ETHICS RULE** prohibits appraisers from communicating misleading reports. Simply changing the client name on the report cannot change or replace the original appraiser-client relationship. This act is misleading. Further, the appropriate scope of work for any assignment can only be developed after identifying a client, other intended users, and the intended use of the appraiser's opinions and conclusions at the time of the assignment. It is also likely that when an appraisal report has been readdressed to a client different from the original client, it will not serve the second client's intended use, since there is no way the appraiser could have developed an appropriate scope of work for the new assignment after the fact. The appraiser, based on communication with the client at the time of the assignment, must determine the intended use and intended users. They cannot be altered retroactively.

AO-27, *Appraising the Same Property for a New Client*, and **AO-26**, *Readdressing (Transferring) a Report to Another Party*, reinforce these concepts.

Example F

An appraiser was recently asked to update an appraisal performed by another appraiser who works for a different appraisal company. Can the appraiser prepare an update if another appraiser performed the original appraisal?

Response

Yes. **Advisory Opinion AO-3**, *Update of a Prior Assignment*, provides guidance on how such an assignment can be performed in conformance with USPAP. Regardless of the terminology used, when a client seeks a current value or analysis of a property that was the subject of a prior assignment, it is not an extension of the prior assignment, but is simply a new assignment. An "assignment" is defined in USPAP as: *A valuation service provide as a consequence of an agreement between an appraiser and a client.*

Example G

A certified residential real property appraiser's business has been slow lately and she occasionally has the opportunity to perform commercial appraisals with a certified general real property appraiser. To date, she has only been involved with the preparation of a few small commercial properties. However, the appraiser recently received a call from a client for a fee quote on a full-service car wash. Since she has prepared appraisals on other commercial properties, she believes she can adequately prepare an appraisal on a car wash facility. May she take the assignment? Does her being a certified residential appraiser affect her taking the assignment?

Response

The first question cannot be simply answered with a yes or no. A full-service car wash is considerably different from a small commercial property, and it would involve a much more complex valuation assignment. The car wash also includes tangible personal property, such as equipment, and possibly intangible personalty, such as an assembled workforce and capitalized economic profit. These elements of the valuation are covered by **STANDARDS 7–10**. Therefore, before accepting the assignment, the appraiser must disclose her lack of knowledge and/or experience. She also must take all steps necessary to complete the assignment competently and describe the circumstances in the report (refer to the **COMPETENCY RULE**).

To answer the second question, appraisers must check their own applicable state real property appraisal laws, since the property type is general in nature and, therefore, typically outside the definition of property types covered for a state certified residential appraiser.

Example H

The property owner’s attorney in a condemnation case has asked a real property appraiser to invoke the **JURISDICTIONAL EXCEPTION RULE** of USPAP in a particular commercial property case. **Standards Rule 1-5** requires appraisers to analyze any prior sales of the property being appraised that occurred within three years. The subject property sold within one year of the appraisal for what everyone admits was a very low price, although all parties claim the sale was not made under duress. For this reason, the attorney does not want the prior sale mentioned in the appraisal report; however, the appraiser reviews USPAP with the attorney, showing him **Standards Rule 1-5** (which prohibits departure) and the definition of *binding requirements* in USPAP. The attorney is aware that the **JURISDICTIONAL EXCEPTION RULE** exists and tells the appraiser to invoke it for this situation. How should the appraiser respond?

Response

Standards Rule 1-5, which concerns the analysis of prior sales, is a binding requirement and cannot be departed from unless the **JURISDICTIONAL EXCEPTION RULE** is applicable. It is not invoked at the client’s discretion. The **JURISDICTIONAL EXCEPTION RULE** is not applicable unless the requirements of USPAP are contrary to the law or public policy of a jurisdiction. In this example, since the attorney does not cite a specific law or public policy in the jurisdiction that is applicable to the issue and demonstrates the contradiction with **Standards Rule 1-5**, the Rule does not apply. If it did apply, the report would have to disclose that the **JURISDICTIONAL EXCEPTION RULE** was applied and cite the specific legal authority as well as the specific USPAP requirement(s) being disregarded.

Also, as a technical matter, one does not “invoke” the **JURISDICTIONAL EXCEPTION RULE**. A jurisdictional exception is a condition of an assignment—i.e., it just happens—it is not a choice made by either the appraiser or the client.

Example I

A client recently asked a certified residential appraiser to reduce his fee for appraisals in instances where the loans do not close. The client indicated he would be willing to pay extra for other assignments in return. Would this practice be ethical?

Response

No. The **Management** section of the **ETHICS RULE** states, in part,

It is unethical for an appraiser to accept an assignment or to have a compensation arrangement for an assignment that is contingent upon ...

- 5. the occurrence of a subsequent event directly related to the appraiser's opinions and specific to the assignment's purpose.*

As with the other related prohibitions in this section of the **ETHICS RULE**, such contingencies are not allowed because they can inspire unethical behavior and erode public trust in professional appraisal practice. The fact that the “lost” fee could be “made up for” in other fees does not change the interpretation. **Standards Rules 2-3, 8-3, and 10-3** also require appraisers to state that their compensation for completing an assignment is not contingent upon a subsequent event.

Example J

A personal property appraiser has prepared an appraisal of the personal property in an estate and plans to charge a fee based upon the aggregate value of the estate properties appraised. Does USPAP permit the appraiser to structure his fee in this way?

Response

No. The **Management** section of the **ETHICS RULE** states, in part,

It is unethical for an appraiser to accept an assignment or to have a compensation arrangement for an assignment that is contingent upon...

- 3. the amount of a value opinion.*

Standards Rules 2-3, 8-3, and 10-3 also requires an appraiser to state that their compensation for completing an assignment is not contingent upon an amount of a value opinion.

Example K

A client asked an appraiser to eliminate a cost approach in an appraisal assignment of a newer house, but not to prepare a Limited Appraisal. The appraiser concludes that the cost approach, although applicable, is not necessary to produce credible conclusions. He is unsure, since he considered the approach, whether the assignment is a Complete or Limited Appraisal. He is also uncertain whether he should include a cost approach in his workfile although he is not performing the approach to value in his appraisal. Is the assignment considered a Complete Appraisal or a Limited Appraisal? Is he required to include the omitted approach in his workfile?

Response

The appraiser may do a Limited Appraisal, as he has concluded that the specific requirements are applicable but not necessary; therefore, invoking the **DEPARTURE RULE** is appropriate. However, if the appraiser had concluded that the cost approach was NOT applicable, then departure would not be necessary and he would be doing a Complete Appraisal. If the cost approach is applicable and necessary, then departure would not be allowed, and the appraiser

would be required to complete the approach even though the client is not requesting it in the assignment.

The appraiser is confused, however, about the need to include the methods in his workfile. Departure means he does not do them at all, not even for the workfile.

Example L

An appraiser just received an assignment that involves a city lot that is improved with two residences. The client has requested that he appraise the site and only the main residence, without mentioning the other structure. The appraiser is unsure how to proceed and wonders if it is ethical to accept this assignment. Does USPAP permit him to accept the assignment as requested?

Response

No, it is not ethical to accept the assignment as outlined without proper disclosure. The **Conduct** section of the **ETHICS RULE** states:

An appraiser must not communicate assignment results in a misleading or fraudulent manner. An appraiser must not use or communicate a misleading or fraudulent report or knowingly permit an employee or other person to communicate a misleading or fraudulent report.

Performing an appraisal without disclosing the existence of both structures in the report would be misleading.

Example M

A certified general appraiser recently developed and orally reported a Complete Appraisal of a hotel's real property as part of a tax appeal. The opposing attorney, under discovery, requests the appraiser's workfile, which will include his signed certification. The appraiser is amused, as he put nothing in writing specifically to avoid having to show it to the opposing side. Is he in compliance with USPAP?

Response

No. The answer to the question is found in the **Record Keeping** section of the **ETHICS RULE**. It applies to oral reports as well as written reports, and specifically requires a signed certification and all documentation necessary to support the appraiser's opinions and conclusions. The **Record Keeping** section states, in part:

The workfile must include: ...

- *summaries of any oral reports or testimony, or a transcript of testimony, including the appraiser's signed and dated certification; and*
- *all other data, information, and documentation necessary to support the appraiser's opinions and conclusions and to show compliance with this Rule and all other applicable Standards, or references to the location(s) of such other documentation.*

Example N

An attorney client has requested a “Limited-Summary Appraisal” from a certified general appraiser. The appraiser wants to comply and he completes the assignment based on what he understands these terms to mean, using only minimum research. He is careful to write “Limited-Summary Appraisal” on the title page because he is sure this is a USPAP requirement. Is this correct? What are the USPAP requirements concerning types of appraisals and reports?

Response

There are only two types of appraisals, Complete and Limited. There are three types of written reports: Self-Contained, Summary, and Restricted Use. USPAP requires the appraiser to prominently state which report option is used. There is no requirement to state whether the appraisal is Limited or Complete, although when it is necessary to discuss any departure it might be a good business decision to state the appraisal type. In conclusion, the appraiser was correct in citing the USPAP requirement for the type of report: a Summary Appraisal.

The client also might be confused as to the type of appraisal assignment he is requesting. The appraiser needs to communicate with the client to be sure he understands what the specific report type will include, and confirm that such a report type will assist in solving the client’s problem based on the intended use of the assignment results. Communication with the client on this point far outweighs the risk of seeming uninformed.



Suggested Responses to Discussion Examples

Section C—STANDARD 1

Example A

The vice president of 1st Savings Bank in Centertown is reviewing an appraisal of a 450-unit proposed apartment complex completed by a certified general appraiser. The value opinion is based on a very aggressive occupancy projection, yet the report contains no marketability study, and only a brief statement of current vacancy rates with no support for the vacancy conclusion.

The vice president invites the appraiser to his office to discuss the appraisal. At their meeting, the appraiser points out that the client was not willing to pay for a detailed study and that he prepared the appraisal under severe time constraints. Has he made a legitimate argument?

Response

No. In this example, the appraiser failed to properly consider supply and demand, which is an important factor in apartment appraisals. This omission relates to **Standards Rules 1-1(b), 1-2(e), and 1-3(a)**. Fee and time constraints do not excuse an appraiser from compliance with applicable Standards Rules. The failure to properly consider supply and demand may indicate a lack of competency; if so, this situation may also be a violation of the **COMPETENCY RULE**.

Example B

An appraiser works in the Texas office of a national appraisal firm. She was recently sent to Denver to appraise a shopping mall. She spent a day inspecting the property and interviewing the property manager, and then flew to Omaha where she was scheduled to meet with another client.

Back at her office, the appraiser made several calls to Denver appraisers requesting comparable sales and rental data, but she got little information. Instead, she used information on Texas shopping centers that she had on file to complete the appraisal report. Later she received a letter from an FDIC reviewer who was highly critical of her appraisal. He said that she failed to consider several important, relevant sales of Denver-area shopping centers indicating values substantially different from her conclusion. Do the circumstances of her schedule relieve her of the responsibility to learn the nuances of the market? Is the appraiser allowed to do an appraisal in a state in which she has no experience?

Response

The appraiser did not spend enough time in the Denver area to understand the local market and obtain the necessary data to complete the appraisal competently. Therefore, she violated **Standards Rule 1-1(b)**, the **Comment**, which requires an appraiser to *ensure that data that would have a material or significant effect on the resulting opinions or conclusions are identified and, where necessary, analyzed*.

Standards Rule 1-4 requires an appraiser to *collect, verify, and analyze all information applicable to the appraisal problem, given the scope of work identified in accordance with Standards Rule 1-2(f)*. (Bold added for emphasis) The appraiser's scope of work decision, discussed under **Standards Rule 1-2(f)**, was flawed as she did not conduct sufficient research to appraise the subject of the assignment in its locality and, thereby, become competent to identify

and analyze relevant sales. Finally, the **COMPETENCY RULE** sets forth the appraiser's responsibility with regard to appraising properties in geographic areas where she does not have recent experience. The appraiser is allowed to undertake this type of assignment, as long as she complies with identified responsibilities set forth in the **COMPETENCY RULE**, which include the disclosure of the steps taken to become competent.

Example C-1

The client is a major developer of ski resorts. He has contacted an appraiser and asked him to provide an opinion of the market value of the total assets of a resort he is considering purchasing. The client emphasizes that he is not interested in an allocation of the assets among the categories tangible real, tangible personal, and intangible property. The appraiser is confused. He is certain that USPAP requires him to allocate or separately value the non-realty items. Is he correct? Must he allocate the total assets? Is it appropriate for him to accept the assignment?

Response

No allocation is necessary in this case, given the intended use and intended user. **Standards Rule 1-4** specifies separate valuations when the extent of the scope of work would demand it and further addresses competency issues in personal property appraisal (**STANDARD 7**) or business appraisal (**STANDARD 9**). The appraiser could accept the assignment as described by the client, as long as he concludes that it is the appropriate scope of work, given the intended use. Again, the burden of proof is on the appraiser to provide credible assignment results in the context of the intended use. The client may request a certain scope of work, but the appraiser is responsible for making the appropriate decision.

Example C-2

A local hotel developer has applied for a permanent loan on his hotel. The lender has contacted a certified general appraiser and requested an appraisal. The intended use is underwriting a real estate loan. The loan officer has requested the market value of the total assets with no allocation among the components. He has told the appraiser to "just call it market value of the hotel." Must the appraiser allocate the assets in this case?

Response

Yes. The intended use, to assist the lender in making a real estate loan decision, would require allocation. In this case, simply describing the value as "market value of the hotel" and not providing an allocation would be potentially misleading. **Standards Rule 1-4 (g)** applies in this situation, as does the **Comment**. The mortgage will be placed on the real property component and the effect on value of the trade fixtures, personal property, and intangible items must be discussed. A separate appraisal is required when the value of a non-realty item or combination of such items is significant to the overall value.

Example D

An appraiser is retained by Stillwater Bank to review values of the real property that serve as collateral for the loan portfolio of Valley Bank, a small banking association that Stillwater wants to acquire. An appraiser with many years of residential experience has done most of Valley's appraisal work.

All the appraisals are completed on a URAR. The number of minor errors and inconsistencies the review appraiser finds in almost every report troubles her. The value opinions, however, are accurate. The appraiser seems annoyed when confronted about the quality issue. He stresses that USPAP does not require perfection. Is he correct?

Response

The appraiser appears to have rendered appraisal services in a *careless or negligent manner* and, therefore, violated **Standards Rule 1-1(c)**. Although perfection is not the goal of USPAP, competence, reasonable care, and diligence are required. The series of individually insignificant errors diminishes the credibility of the results.

Example E

A residential appraiser offers the quickest turnaround and the lowest fees in town. In order to do this she has become very efficient. She completes her property inspections in 10 minutes, using the city assessor's database for the site and building dimensions, and enters data on the subject property directly into her laptop computer on the site. Her comparable sales with color photographs come directly from the MLS database and she does not inspect them. It is not unusual for her to complete 10 appraisals a day and electronically transmit them to her clients.

Recently, two of her appraisals have come under fire. In one case, her best comparable was sold under duress, a situation that would have been revealed by verification with a participant to the transaction. Another comparable is in a neighborhood that is in an entirely different price range from the subject, but this fact was not revealed in the report. In another appraisal, the size of the subject was actually 400 square feet different from that reported in the city assessor's records and affected the property value. The appraiser explained that there is no way she can measure each subject property, look at all the comparables and talk to a participant, and still meet her turnaround commitments, much less earn a respectable fee. Is she required to measure the subject improvements and inspect and verify her comparables?

Response

USPAP does not require either an inspection or verification of the improvements of a subject property; such a request is directed by the client in the context of the intended use of the assignment results.

The example does not specify the intended uses of the appraisals in question. In order to determine the appropriate scope of work for any assignment, the appraiser must first identify the client, other intended users, intended use, type and definition of value, effective date, and relevant property characteristics pertaining to the assignment.

Appraisers are required by **Standards Rule 1-1(b)** to *not commit an error of omission or commission that significantly affects an appraisal*. This rule requires the appraiser to gather factual information in a manner that is sufficiently diligent. **Standards Rule 1-1(c)** requires appraisers to *not render appraisal services in a careless or negligent manner*. Appraisers must use due diligence and due care in performing appraisal services, including gathering actual data such as square footage.

Standards Rule 1-4 requires the appraiser to *collect, verify, and analyze all information applicable to the appraisal problem, given the scope of work identified in accordance with Standards Rule 1-2(f)*. (Bold added for emphasis) It also requires, in situations where the sales comparison approach is applicable, analysis of such comparable sales data *as are available*.

The term *verify* is not defined in USPAP and means different things to different appraisers. The scope of work decision is a function of expectations of participants in the market for similar appraisal services and what the appraiser's peers' actions would be in performing similar assignments. If the intended use is to assist in making a loan decision, then inspection of the comparables would more than likely be necessary. The level of verification must be such that a credible appraisal conclusion is possible given the intended use.

Example F

A real property appraiser has been asked to appraise a surplus parcel of land at market value. The date of the appraisal will be prior to its advertisement for sale by the local community public works department. According to the public works director, a covenant will be placed on the land immediately prior to the sale that will restrict its use to open space or recreation. The value opinion in the appraisal is to reflect the title condition. The property is in use by the public works department and the use limitation is not in place. Since the appraiser knows the "as is" condition of the property title is not as the director indicated, can he do the appraisal as if the covenant were in place? If so, which is involved in the assignment, an extraordinary assumption or a hypothetical condition?

Response

Yes, he may do the assignment. Given the type and definition of value of the appraisal (market value, with the title conditioned as the director described), and intended use of the assignment results (provide the client with information for use in deciding an asking price), the appraisal must reflect an analysis as though the covenant were in place.

The appraisal of the property as though the covenant were in place requires a hypothetical condition in the appraisal because, as of the date of appraisal, the property did not have the covenant. According to **Standards Rule 1-2(h)**, the hypothesis must be clearly disclosed in the appraisal report, the assumption of the hypothetical condition must be clearly required for legal purposes, for purposes of analysis (as it is here), or for purposes of comparison, and not be misleading; and the report must clearly describe the rationale for the assumption and the nature of the hypothetical condition.

The distinction between a hypothetical condition and an extraordinary assumption is that the former represents a situation that is contrary to what actually exists. The extraordinary assumption presumes as fact otherwise uncertain information which, if found false, could alter the opinions or conclusions.

Example G

An appraiser has been asked to value an eight-house subdivision, which has yet to sell a single unit. All eight houses are the same model, so the appraiser prepares one URAR, then multiplies the value conclusion by eight and reports the product as his conclusion of the market value of all eight houses. He has been told that he may do the assignment this way as long as there are fewer than 10 units involved. Is this acceptable?

Response

Standards Rule 1-4(e) states that an appraiser must not develop an opinion of value for a whole property merely by adding together the values of its component parts. The fact that fewer than 10 houses are involved has nothing to do with the appropriateness of the method. In this case the market value of all eight houses is likely less than the sum of the individual values, as selling costs, profit, carrying costs, etc., would need to be deducted. **Standards Rule 1-1(a)** might also apply in terms of the use of appropriate methods and techniques for this complex assignment.

Example H

Appraiser A has been retained to appraise a 45-acre parcel in Hopeville for a local property owner as of a retrospective date two years ago. He prepares a Self-Contained Appraisal Report that includes eight land sales; most of these properties are in far superior locations on the main commercial street in Hopeville, and no adjustment is made for this fact. He concludes that the parcel has a market value of \$6,500,000.

Appraiser B, an appraiser for the Fifth Bank of Hopeville, is looking over Appraiser A's appraisal. Something is familiar, but she cannot quite place it. Suddenly it comes to her. She finds a clipping in her files indicating that the court approved a sale of the same 45-acre parcel for \$2,600,000 in cash. The property was on the market for 18 months, a full listing sheet was widely distributed, and the court found that the price was fair. The sale settled three months after the retrospective date of value.

When asked about it, Appraiser A explains that, although he was aware of it, USPAP does not require reporting a sale that occurs after the **effective** date of value. What are the correct reporting responsibilities applicable in this situation? Are there other potential problems with the assignment?

Response

Standards Rules 1-5(b) and 2-2(a-c)(ix) discuss the requirements relating to sales history. The appraiser is required by **Standards Rule 1-1(b)** to *not commit a substantial error of omission or commission that significantly affects an appraisal*. It is the responsibility of the appraiser to ensure that data that would have a material or significant effect on the resulting opinions or conclusions are identified and, where necessary, analyzed.

Yes. Although the sale settled after the effective date of the appraisal, its list price—and perhaps contract price and terms—still need to be analyzed and reported. **Statement No. 3 (SMT-3), Retrospective Value Opinions**, is also applicable.

In addition, this appraisal might involve violations of the **Conduct** section of the **ETHICS RULE** concerning impartiality, advocacy, or communicating assignment results in a misleading manner.

Example I

A licensed residential appraiser is appraising a single-family residence for a lender. His conclusion is a market value of \$200,000. He dutifully notes that the property sold two years ago for the same amount, and has been listed for six months at \$199,999. So far, no takers have emerged. Comment on the appraiser's compliance with USPAP.

Response

Standards Rule 1-5 requires the appraiser *analyze all agreements of sale, options, or listings of the subject property current as of the effective date of the appraisal.* (Bold added for emphasis.) Simply reporting the history is not enough. In this case, without analysis the history seems to suggest the \$200,000 estimate is too high.

Example J

In reading his state's newsletter regarding disciplinary actions against appraisers, an appraiser notices many such actions are related to flipping schemes. Being a newly certified appraiser, he is wondering what kinds of things appraisers should do to avoid being inadvertently entangled in such schemes. How does USPAP assist in this matter?

Response

Flipping schemes are typically based on inflated values provided by an appraiser. There are a number of actions appraisers can take to safeguard against completing an inflated appraisal. **Standards Rule 1-5** requires appraisers to analyze all current agreements of sale, options, or listings of the subject property, when such information is available in the normal course of business. Many lenders require that agreements of sale be provided to the appraiser for review and analysis. Verifying the terms of sales with assessing officers or listing agents/brokers may reveal multiple transactions on the same property. Sometimes the second or third leg of a flip can be discovered when the seller in the sale agreement is not the owner of record.

Experienced appraisers can recognize anomalies in the market and avoid relying on sales that are not reflective of the market. If asked to value a property in an unfamiliar geographic area, an appraiser should become familiar with the area and the market for the subject property. The **Comment** to the **COMPETENCY RULE** should be reviewed in this instance.

Standards Rule 1-4 requires the appraiser to collect, verify, and analyze information applicable to the appraisal problem. Identifying the conditions of sale, financing terms, and motivations of the buyer help the appraiser to adjust sales to the market and avoid the affects of inflated values.

Standards Rule 1-2(e) requires the appraiser to identify the characteristics of the property that are relevant to the type and definition of value and intended use of the appraisal. These characteristics include location and physical, legal, and economic attributes. Such knowledge is critical in the valuation process. Appraisers should exercise care in identifying these attributes, noting any adverse condition that affect the property's value.

Suggested Responses to Discussion Examples

Section C—STANDARD 2

Example A

An appraiser is requested to perform a Complete Appraisal and submit a Self-Contained Appraisal Report. The letter of transmittal and other sections of the document identify the report as such. In the appraisal report, the appraiser briefly *summarizes* the highest and best use section. However, the approaches to value are extremely detailed and meet the requirements of a Self-Contained Appraisal Report. Has she satisfied the requirements for a Self-Contained Appraisal Report?

Response

This example addresses the definitions and requirements of **Standards Rule 2-2**, especially the differences between the terms *describe*, *summarize*, and *state*. The content requirements of each report option must be complied with 100%; otherwise, the entire report falls into a lesser requirement reporting option. If any report section is less than what is required by the specific option selected, then the entire report must be identified as that reporting option. In this instance, **Standards Rule 2-2(a)(x)** requires the appraiser to *describe the support and rationale for the highest and best use of the real estate*. (Bold added for emphasis.)

Example B

Client X is responsible for ordering and reviewing appraisals prepared for a Thai company that is investing in properties in the United States. He retained a certified general appraiser in the United States to value a shopping center that his company was about to purchase. He explained in a letter the importance of having a detailed report since he would be in Thailand when he reviewed the appraisal. The two never had an opportunity to talk, however. When he received the appraisal report, the comparable data were summarized with a brief statement of the appraiser's conclusions. Client X is very unhappy. What part of USPAP is intended to avoid this type of miscommunication?

Response

Obviously, by the description of the client's request, he needed a Self-Contained Appraisal Report. The appraiser, however, appears to have rendered either a Summary or a Restricted Use Appraisal Report. Even if the report clearly and accurately identifies the report option used, there may be a violation of **Standards Rule 2-1(b)**, which requires that the report *contain sufficient information to enable the intended users of the appraisal to understand the report properly*. In addition, by submitting this type of report, the appraiser may have violated the contract for services with the client. Written contracts are important, although they are not required by USPAP. Even when written contracts specifically identify the type of appraisal (Complete or Limited) and the type of report (Self-Contained, Summary, or Restricted Use), extreme care should be taken in communication with the client.

Example C

A mortgage broker hired an appraiser to prepare an appraisal on a single-family property. He asked that she discuss her value opinion with him orally prior to transmitting the report. The appraiser completed her analysis and telephoned the client with her conclusions. The broker client was indignant and objected strongly to the value conclusion, indicating that the “figure” would not help his client’s objectives. He further indicated that there would be no need to provide a written report. What are the appraiser’s obligations under USPAP?

Response

Clearly, the reporting of the value conclusion to the mortgage broker client is an oral report. A summary of such a report, along with the appraiser’s signed and dated certification, must be included in the workfile. Reference is made to **Standards Rule 2-4**, which indicates that an oral appraisal must meet the substantive matters addressed under a Summary Appraisal Report (**Standards Rule 2-2 (b)**).

The client does not have to take delivery of the written report. The appraiser has met the assignment conditions by completing the appraisal and providing an oral report and maintaining a workfile for the assignment. The workfile must be retained for the specified period noted in USPAP.

Example D

A bank hires a certified residential appraiser to provide residential appraisals and requires that he sign all reports completed for the client by his company.

The bank recently underwent a regulatory examination and was cited for poor quality appraisals. The senior loan officer called the appraiser and complained. The appraiser was quick to point out that he signs on the right side of the URAR under the signature block entitled, “Supervisory Appraiser” and checks the “did not inspect property” box. He explains that he cannot be held responsible for errors made by his staff appraisers, most of whom are trainees. Is he correct?

Response

No. The **Comment** to **Standards Rule 2-3** states that regardless of the qualifying language, any appraiser signing the certification—which is the case here because the appraiser signed the report—accepts full responsibility for all elements of the report.

Example E

A new residential appraiser recently ordered appraisal form software and isn’t sure what to do, as the current software available does not address the most recent USPAP changes. What should she do?

Response

Appraisers are required to supplement an appraisal form when the form lacks required elements. This requirement can be found in the **Comment** to **Standards Rule 2-2**. Appraisers should take the appropriate steps to ensure that their reports comply with the current version of USPAP.

Example F

An appraiser has five appraisers whom he supervises and he spends long hours inspecting properties as a result. He often is away from the office when it is time to transmit an appraisal report to a client, so his assistant signs his reports. Does this create any USPAP issues?

Response

USPAP does not specifically state that the appraiser must personally sign a report. The **DEFINITIONS** section of USPAP states that a signature is *personalized evidence indicating authentication* and the **Comment** requires the appraiser to have *sole personalized control of affixing the signature*.

Standards Rule 2-3 states, *Each written real property appraisal report must contain a signed certification...*

In the **DEFINITIONS** section of USPAP, a *signature* is defined as:

personalized evidence indicating authentication of the work performed by the appraiser and the acceptance of the responsibility or content, analyses, and the conclusions in the report.

Comment: *A signature can be represented by a handwritten mark, a digitized image controlled by a personalized identification number, or other media, where the appraiser has sole personalized control of affixing the signature.*

Unless specifically contrary to the law of a particular jurisdiction, USPAP allows another person to sign for an appraiser, as long as it is with the appraiser's specific authorization and is not misleading. One solution would be for that other person to sign the appraiser's name and then write his or her own initials along side the signature, preceded by the word "by" (for example, by "skb").

Example G

An appraiser has been asked by a client to prepare a Restricted Use Appraisal Report and the client has identified in communication with the appraiser that other intended users will also receive the report. Does USPAP allow the use of this report option in such a circumstance?

Response

No. The **Comment** to **Standards Rule 2-2** states that *when the intended users do not include parties other than the client, a Restricted Use Appraisal Report may be provided*.

In other words, this report option may only be used when the client is the only intended user in the context of the intended use.

The reason underlying this use restriction is that the client is assumed to have a sufficient level of knowledge to enable him or her to understand a report of this type. If other intended users were to be given such an abbreviated report, they could easily misunderstand it and potentially be misled.

END OF  SECTION

Suggested Responses to Discussion Examples

Section D—STANDARD 3

Example A

A review appraiser with a busy litigation practice takes great delight in criticizing every work product he is handed, always citing USPAP violations. He proudly boasts of “never finding an appraisal he couldn’t tear apart.” He confidently prepares his USPAP critique before ever seeing the appraisal to be reviewed, then just drops in the facts. Discuss the potential issues relating to the appraisal review approach taken by this review appraiser.

Response

The attitude expressed by the review appraiser suggests possible violations of the **ETHICS RULE**, in which the requirements for performance *with impartiality, objectivity, and independence, and without accommodation of personal interests* appear. An appraiser must not perform as an advocate for any party or issue, or accept an assignment that includes reporting of predetermined opinions and conclusions.

Example B

A reviewer for All-Purpose Bank has reviewed real property appraisals for many years. His supervisor has requested that he review an industrial appraisal that includes a substantial amount of fixtures and equipment in addition to the real estate.

What Standard should be used for this review? Does the **COMPETENCY RULE** apply in this case?

Response

The review should be performed using **STANDARD 3**, which was expanded effective January 1, 2003, to include reviews in **all** appraisal disciplines—real property (including mass appraisal), personal property, and business or intangible assets. The **COMPETENCY RULE** also applies because the reviewer apparently has no experience in personal property appraisal or performing an appraisal review.

Example C

Appraiser A, a state certified general appraiser, works as a staff appraiser/reviewer for the First of All Bank in Centertown. Her boss has asked her to review a Self-Contained Appraisal Report on the Peach Blossom Office Center prepared by Appraiser B, a fee appraiser. Appraiser A is to review the appraisal prepared by Appraiser B and provide the bank with her value opinion based on the contents of Appraiser B’s appraisal report. Appraiser A is uncertain whether she can accept this assignment without inspecting the subject and comparable properties, verifying the information in the report, and conducting her own, independent data search and analysis.

What is she required to do? How would her role and responsibilities change if the reporting option were a Restricted Use Appraisal Report? Would her responsibilities change if the client only wanted her to “concur or not concur” with the value?

Response

The appraiser may accept this assignment if she prepares an appraisal review report in accordance with **STANDARD 3** that clearly discloses the scope of work to be performed (what she did do, and if appropriate, what she did not do).

Under **Standards Rule 3-1(c)**, when the scope of work includes the reviewer providing her own value opinion, the following applies:

- The reviewer's scope of work in developing her value opinion may be different from that of the work under review.
- The effective date of the reviewer's opinion of value may be the same or different from the date of the work under review.
- The reviewer is not required to replicate the steps completed by the original appraiser.
- Those items in the work under review that the reviewer concludes are credible and in compliance with the applicable development Standard (**STANDARD 1**, in this case) can be extended to the reviewer's value opinion development process on the basis of an extraordinary assumption by the reviewer.
- Those items not deemed to be credible or in compliance must be replaced with information or analysis by the reviewer, developed in conformance with **STANDARD 1** (in this case) to produce a credible value opinion.
- The reviewer may use additional information available to her that was not available to the original appraiser in the development of her value opinion; however, the reviewer must not use such information as the basis to discredit the original appraiser's opinion of value. The **Comment** to **Standards Rule 3-1(c)** describes appropriate methods for indicating the precise extent of the review process. See also **Standards Rule 3-1(g)** in conjunction with this example.

Additional guidance is provided in **AO-20**, *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*. If the report had been a Summary Appraisal Report, the information available to complete her own opinion of value might be insufficient, depending upon the extent of the summarization.

If the report were a Restricted Use Appraisal Report, Appraiser A could not reasonably develop an opinion of value without access to the assignment workfile.

Wording such as "I concur with the value" or "I agree (or disagree) with the value" represents an appraisal and, therefore, involve **STANDARD 1**. Wording such as "the value opinion stated in the appraisal report is (or is not) adequately supported" might be used in an appraisal review report that does not express an opinion of value. These concepts, including appropriate language examples, are discussed in **AO-20**.

Example D

An appraisal reviewer for the Bank of Centerville prepares written reviews of commercial appraisals developed for the bank on properties with values in excess of \$1,000,000. The bank's policies require all reviewers to comply with **STANDARD 3** and to reject any appraisal that is not within 5% of the reviewer's opinion of value. Can an appraiser perform such a review assignment under USPAP? If so, what must the review appraiser do?

Response

Yes. **STANDARD 3** does not require an appraisal reviewer to develop an appraisal as part of the review function. However, in many cases clients expect reviewers to provide their own opinion of value. In this case, the client is requiring the reviewer to provide an *appraisal* in addition to a review. (Refer to the use of "benchmarks" and "ranges" in the **Comment** to the definition of the term *appraisal*.) This type of assignment is permitted under **STANDARD 3**.

STANDARD 3 provides guidance on what a reviewer must do to complete such an assignment. A key issue is the importance of identifying the appropriate scope of work and verifying with the client that both a review and an appraisal are being requested. See **Standards Rule 3-1(c)**; reviewers are cautioned when performing this type of service to be clear about their scope of work when developing both the review and the appraisal. Additional guidance is provided in **AO-20**, *An Appraisal Review Assignment that Includes the Reviewer's Own Opinion of Value*.

Example E

A certified appraiser has been asked by a government agency to review two appraisals of the same real property and reconcile them to a single value. Can she perform this assignment under USPAP?

Response

Yes, she can perform this assignment under USPAP. The assignment constitutes a real property appraisal review assignment, which includes both an appraisal review and an appraisal. **STANDARD 3** addresses the development and the reporting of an appraisal review assignment. The specific appraisal review requirements of **Standards Rule 3-1** and **Standards Rule 3-2** apply to both appraisals being reviewed. The appraiser could provide her own opinion of value in accordance with **Standard Rules 3-1(c) and 3-2(d)**.

In this type of situation it would be appropriate to include the results of her review of both appraisals and her own value opinion in the same appraisal review report for proper understanding of the assignment and thus not be misleading. A single signed certification would be provided in accordance with **Standards Rule 3-3**.

Example F

A certified appraiser reviews many residential appraisals for a major lender. He has found numerous errors in several reports prepared by the same appraiser. He believes the errors are intentional and caused the value conclusions to be inflated in several instances. He has discussed the matter with his client but is also wondering if he is permitted by USPAP to file a complaint with the state appraiser board (where the appraiser is licensed) without his client's consent. Is he permitted to do so?

Response

Absent any higher precedent law or regulation, a reviewer may file a complaint with a state appraiser board without the consent of his or her client.

The **Confidentiality** section of the **ETHICS RULE** states that:

An appraiser must protect the confidential nature of the appraiser-client relationship.

The **Confidentiality** section also states:

*An appraiser must not disclose confidential information or assignment results prepared for a client to anyone other than the client and persons specifically authorized by the client; **state enforcement agencies** and such third parties as may be authorized by due process of law; and a duly authorized professional peer review committee except when such disclosure to a committee would violate applicable law or regulation. (Bold added for emphasis.)*

END OF SECTION



Suggested Responses to Discussion Examples

Section E—STANDARDS 4 and 5

Example A

A client asks an appraiser to review an appraisal report that was prepared by another appraiser. The client only wants an opinion of the quality of the original appraisal report, and does not want the appraiser to develop a separate value opinion. May the client's request be treated as an appraisal consulting assignment under **STANDARDS 4 and 5**?

Response

No. This is an appraisal review assignment that should be completed in compliance with **STANDARD 3**. The **Comment** to **STANDARD 4** specifically states, *...an opinion as to the quality of another appraiser's work cannot be the purpose of an appraisal consulting assignment.*

Example B

A real estate developer contacts a certified general appraiser and asks him to develop opinions as to the current market value of five different unit types that are being considered for a new development. In addition, the developer wants the appraiser to perform a market study to determine what mix of unit types would yield the fastest projected absorption rate. Which Standards apply?

Response

The value opinions developed for the unit types are appraisals that should be developed in compliance with **STANDARD 1** and communicated in compliance with **STANDARD 2**. The market study is appraisal consulting. This task should be developed in accordance with **STANDARD 4** and communicated in compliance with **STANDARD 5**.

Example C

A client wants advice about how she might maximize her vacant warehouse property's potential. She engages the services of a state certified appraiser to develop a recommendation regarding whether she should demolish the improvement or redevelop it. Does the advice constitute an appraisal or an appraisal consulting assignment?

Response

This assignment is an appraisal consulting assignment although the recommendations to the client will include at least one opinion of value as a component of the analysis leading to the assignment results.

As the **Comment** to **STANDARD 4** states:

Real property appraisal consulting assignments encompass a wide variety of problems to be solved. However, the purpose of an assignment under this Standard is always to develop, without advocacy, an analysis, recommendation, or opinion where at least one opinion of value is a component of the analysis leading to the assignment results.

Example D

An appraiser has been asked by a client to appear before the local Planning Board and assist him in obtaining a zoning change. The appraiser is to use an appraisal that the client has already had performed by another appraiser. The appraiser tells the client he will charge him by the hour for this service. Is this assignment an appraisal review, an appraisal consulting service, or a service that does not fall under USPAP? Is it okay to charge “by the hour,” or is this practice considered some kind of contingent fee?

Response

In order to determine the appraiser’s obligation, it is necessary to understand the nature of his role. If he is acting as an appraiser and is expected by his client to act as an appraiser, his services are part of appraisal practice and the ethics and competency requirements of USPAP apply.

This service is a part of appraisal practice under USPAP. The **Comment** to **STANDARD 4** states:

...the purpose of an assignment under this Standard is always to develop, without advocacy, an analysis, recommendation, or opinion where at least one opinion of value is a component of the analysis leading to the assignment results.

This same **Comment** goes on to state:

The ETHICS and COMPETENCY RULES apply to the appraiser performing an appraisal consulting assignment. Appraisers practicing under this Standard must perform the assignment with impartiality, objectivity, independence, and without accommodation of personal interests.

As long as it is performed without advocacy, this service is a real property appraisal consulting assignment that is subject to the requirements of **STANDARDS 4 and 5**. Otherwise, if performed with advocacy, it is a service that falls outside of USPAP, and the appraiser must be extremely careful not to misrepresent his role—i.e., he should understand the expectations of his client—not to act as an appraiser. Therefore, the services he will render will be with bias for his client, and he will not be functioning as an appraiser. He must use extreme care to distinguish that role from other roles that would carry an expectation of being impartial, objective, and independent, i.e., acting as an appraiser.

It is acceptable to charge by the hour. A review of the following unethical practices in the **Management** section of the **ETHICS RULE** indicates that such a practice **does not** constitute any kind of contingent fee:

*It is **unethical** for an appraiser to accept an assignment, or to have a compensation arrangement for an assignment, that is contingent upon any of the following:*

- 1. the reporting of a predetermined result (e.g., opinion of value);*
- 2. a direction in assignment results that favors the cause of the client;*
- 3. the amount of a value opinion;*
- 4. the attainment of a stipulated result; or*
- 5. the occurrence of a subsequent event directly related to the appraiser’s opinions and specific to the assignment’s purpose. (Bold added for emphasis.)*

Example E

Certified Appraiser A has accepted a tax consulting assignment and is to be compensated at one-half of the first year's tax savings. The appraiser completes the assignment, reporting his opinion of market value of the subject property for tax purposes. He clearly discloses his fee arrangement in the letter of transmittal, limiting conditions, and executive summary of his report and also includes a signed certification in accordance with **Standards Rule 5-3**. Is Appraiser A's fee arrangement in conformance with the Standards Rules? Why or why not?

If instead Appraiser A hires an independent appraiser to perform an appraisal for a fixed fee plus an hourly rate for testimony, and Appraiser A charges a contingent fee for presenting and managing the case, would this arrangement be allowed under USPAP? Why or why not?

Response

No. Appraiser A's fee arrangement is in conflict with the **Management** section of the **ETHICS RULE** and with **Standards Rule 5-3**, which prohibits accepting an assignment on a contingent fee basis.

If Appraiser A hires an independent appraiser to perform the appraisal but still charges a contingent fee, he cannot provide the service under USPAP. A contingent fee arrangement is prohibited in the appraiser's certification under **Standards Rule 5-3**. If Appraiser A is not required by law, regulation, or agreement to provide this service under USPAP, then he is free to provide the service as a consultant outside of USPAP and can charge a contingent fee. However, in this case he must not misrepresent the character of his service and should make sure his client and intended users understand that he is not acting as an appraiser or providing the service under USPAP. (See the **ETHICS RULE**.)

Example F

A client has asked real property Appraiser A at an appraisal firm to appraise five proposed model homes in a subdivision. Additionally, the client wants the appraiser to provide a market analysis and recommendations relating to current and proposed supply and demand, marketability, and financial feasibility of the models. The appraiser has the competency to perform the market study, but neither she nor others in the firm currently appraise single-family residences. However, she does know a residential appraiser who is qualified to perform the model home appraisals.

Can Appraiser A accept an assignment like this without appraising the model homes herself? If so, how would she complete it in compliance with USPAP and what are the reporting requirements?

Response

Yes, she can accept the assignment. If Appraiser A, the consulting appraiser, relies on an appraisal performed by another appraiser, the **Comment** to **Standards Rule 4-2(f)** states that the assignment may include a review, prepared in compliance with **STANDARD 3**, of that appraisal. Alternatively, Appraiser A may accept an appraisal from another source as an extraordinary assumption to support the use of the appraisal, as indicated in the **Comment** to **Standards Rule 5-2(h)**.

Example G

In an appraisal consulting assignment, does the consulting appraiser have to perform the appraisal, or can it come from another source?

Response

The source of the appraisal does not matter. The **Comment** to **STANDARD 4** states, *in some assignments, the opinion of value may originate from a source other than the consulting appraiser. In other assignments, the consulting appraiser may have to develop the opinion of value as a step in the analyses leading to the assignment results.*

However, if the consulting appraiser relies on an appraisal performed by another appraiser, the **Comment** to **Standards Rule 5-2(h)** requires the appraisal consulting report to include the information required by **Standards Rule 3-2** or a statement of the appraisal review results or the use of an extraordinary assumption supporting the use of the appraisal.

END OF SECTION



Suggested Responses to Discussion Examples

Section F—STANDARD 6

Example A

An appraiser was recently hired as the assessor for the City of Junctionville and agreed to perform services under USPAP. Owner-initiated appeals in 2003 and 2004 revealed an increasing disparity and inequality in assessment ratios for some commercial properties. These commercial properties were valued using a cost-based model. A sales ratio study indicates performance standards at acceptable levels for all commercial property categories except hotels/motels and apartments. After analyzing the market, the appraiser determines that an income-based model is appropriate for these latter property types and converts the data into the new model. A second sales ratio study reveals that the newly created model results in acceptable performance standards. This new model produced increasing value changes from 30% to 40% for the hotels/motels and apartments, and is used in the 2005 assessment roll.

The owner of two apartment buildings is shocked when his properties' assessed values increased 35%. He appeals to the local hearing authority using appraisal reports prepared specifically for the case that indicate values of 20% less. The hearing authority reduces his assessments to the levels presented in his appraisals. In turn, the owner files a grievance with the City Council alleging the appraiser is incompetent and cites the income-based model she created as flawed. Given this information, did the appraiser violate USPAP?

Response

No. The appraiser developed a model that best reflected the relationship between the values of the properties and their respective supply and demand factors. She also tested the model, which produced overall results within standards of reasonableness. The **Comment** to **Standards Rule 6-6(b)** states:

It is implicit in mass appraisal that, even when properly specified and calibrated mass appraisals are used, some individual value conclusions will not meet standards of reasonableness, consistency, and accuracy. However, appraisers engaged in mass appraisal have a professional responsibility to ensure that, on an overall basis, models produce value conclusions that meet attainable standards of accuracy. This responsibility requires appraisers to evaluate the performance of models, using techniques that may include, but are not limited to, goodness-of-fit statistics, and model performance statistics such as appraisal-to-sale ratio studies, evaluation of hold-out samples, or analysis of residuals.

Example B

The tax day (effective date for assessments) of a township in a state is December 31, for the subsequent year. A property owner has asked the appraiser, who is the deputy assessor, to inspect his property December 1, 2004. He wants her to see that the addition started in October is not yet finished. The appraiser confirms the condition of the subject—the exterior is finished but the interior is still in the stud stage. The owner comments that no work would be done until he returns after New Year's. On December 23, the appraiser receives a final certificate of occupancy and confirmation from the building inspector that the addition is complete. She drives to the property

and, although no one is home, can tell by looking through the windows that the addition is complete. She leaves a note requesting that the owner call her to confirm the interior information.

On January 20, she has yet to receive a call from the owner. She reviews the plans and specifications on file and verifies information with the building inspector. She adds the characteristics to the 2005 assessment roll, noting on the property record card the date of inspection and that the interior elements are based on an extraordinary assumption. The owner subsequently files a complaint with the assessor indicating he is being unfairly treated and the assessment should be based on the appraiser's December 1 physical inspection.

Did the appraiser violate USPAP when she added the addition as completed onto the assessment roll using an extraordinary assumption?

Response

No. Appraisers have the burden of proof that the information used is reasonable and the results of their mass appraisals are credible. The appraiser took the appropriate steps to collect the unknown information pertaining to the addition and correctly employed an extraordinary assumption. The **Comment to Standards Rule 6-4(a)** states:

This Standards Rule requires appraisers engaged in mass appraisal to take reasonable steps to ensure that the quantity and quality of the factual data that are collected are sufficient to produce credible appraisals.

Appraisers complying with **STANDARD 6** have the responsibility to report the date they inspect a property as well as any extraordinary assumptions made that directly affect the appraisal. The appraiser satisfied these requirements.

The appraiser is not required to use the date she inspected the property as her effective date. Her state's statute indicates that December 31 is tax day; therefore, that must be her effective date of appraisal. In this instance, it is irrelevant that she inspected the property on December 1. Additional information that she has determined reasonable and necessary to produce a credible appraisal indicated the property was finished as of December 31. The **Comment to Standards Rule 6-7(g)** indicates that laws, which govern ad valorem taxation, may prescribe the effective date of an appraisal.

Example C

A certified real estate appraiser with extensive experience in mass appraisal has recently begun contacting communities to inquire about providing appraisal services. A county equalization director has been contemplating having some of his communities appraised because they lack uniformity. He is interested in hiring the appraiser's company, but money is tight. The director tells the appraiser that if he can "guarantee" that the appraisal will increase values at least 20% and increase uniformity of assessment, he has the assignment. The appraiser indicates that he is confident he can meet those two objectives, so the director agrees to the terms. The director makes it very clear that the appraiser will only be paid if his appraisal results in the increases. The appraiser takes the assignment.

Is the appraiser violating USPAP by making such a "guarantee" in the assignment?

Response

Yes. The appraiser's intention is to create an appraisal process that *will result* in a targeted 20% increase. He is initiating the engagement without the predispositions required of being impartial, objective, or independent as required under the **Conduct** section of the **ETHICS RULE**.

Creating a model that *will result* in a targeted value conclusion is to produce results that will not be credible for the client's legitimate use. This is a violation of **Standards Rule 6-1(a)**, which states:

...be aware of, understand, and correctly employ those recognized methods and techniques necessary to produce a credible mass appraisal.

The **Management** section of the **ETHICS RULE** is also referenced here in regard to compensation. In this instance, the appraiser is accepting an assignment that is contingent upon the amount of a value opinion.

Example D

The chief appraiser for a city assessor's office specifically prepares the annual values for all the commercial and industrial properties. State statute requires that the properties be appraised as if in fee simple. An owner of several multi-tenant properties in the city is appalled when he receives his assessment notices. He has owned the properties for over 15 years and some of his leases date back to the time he purchased the buildings. The owner calls the appraiser and learns the properties are being valued at market rent levels despite the fact that if he wanted to sell the buildings any purchaser would have to honor the existing lease contracts. The owner's complaint, filed with the city manager, states that the appraiser is not using the appropriate valuation methodologies and techniques for valuing his leased fee interest.

Did the appraiser violate USPAP by valuing the properties using market rent levels rather than contract rents?

Response

No. The appraiser correctly appraised the properties as if in fee simple and unencumbered by existing leases as required by state statute. The **Comment** to **Standards Rule 6-5(c)** states:

*In ad valorem taxation the appraiser may be required by **rules or law** to appraise the property as if in fee simple, as though unencumbered by existing leases. In such cases, market rent would be used in the appraisal, ignoring the effect of the individual, actual contract rents. (Bold added for emphasis.)*

Example E

A retired city assessor decides to open an appraisal company and hires several staff people. His first assignment is with the City of Old Town to perform an appraisal of all its residential properties. The engagement agreement stipulates that the appraisal is to be finished within three years, is to be conducted using the city's mass appraisal software program, and is to be performed in compliance with USPAP. The scope of work identified included physically inspecting and measuring every home.

The appraiser is not familiar with the software program because it didn't come out until after he retired, but since every municipality in the county is now using it he feels it has to be good. He creates a record card for collecting data and splits his staff into two divisions, data collection and date entry. He spends two weeks training his staff in their respective duties.

Near the end of the third year, one of his staff discovers that the record cards being used don't include an area for basement finishes. Therefore, none of the inspecting staff have been identifying whether the properties they inspected had any basement finishes. Because they are out of time, the appraiser decides to simply let the mistake go and finish the project as they have been doing it.

Did the appraiser violate USPAP?

Response

Yes. He violated the following Standards Rules:

Standards Rule 6-1(a): The appraiser did not *understand, and correctly employ those recognized methods and techniques necessary to produce a credible mass appraisal*

Standards Rule 6-1(b): The appraiser *committed a substantial error of omission that significantly affects a mass appraisal.*

Standards Rule 6-3(a), (b): The appraiser did not *identify the appropriate procedures and market information required to perform the appraisal, including all physical, functional, and external market factors as they may affect the appraisal.* Additionally, he failed to use generally recognized techniques as defined in this section.

END OF SECTION



Suggested Responses to Discussion Examples Section G—STANDARDS 7 and 8

Example A

A new personal property appraiser specializes in antiques (properties over 100 years old). He is extremely busy and accepts an assignment from an attorney for an estate, which includes fine china, rare books, and artwork. He delivers a Summary Appraisal Report. The next day the attorney calls him fuming because he has never witnessed such sloppiness. He tells the appraiser that nowhere in his appraisal does he even mention the condition of the items that were appraised.

Is there a problem with the appraisal if condition isn't mentioned?

Response

Yes. The appraiser failed to comply with **Standards Rule 8-2(b) (iii)** indicating that the content of a Summary Appraisal Report must, at a minimum, *summarize information sufficient to identify the property involved in the appraisal, including the **physical and economic property characteristics** relevant to the assignment.* (Bold added for emphasis.)

Physical condition is relevant and material in the appraisal of antiques. The appraiser did not communicate sufficient information for his client's intended use. In a dissolution setting of personal property assets, parties often use the appraisal report to determine other activities as to how, where, and when they are going to dispose of the assets. Condition is a key variable in making many of those decisions.

Example B

For a \$500 fee, a well-respected senior appraiser with 20 years' experience agrees to provide a liquidation value to his client, an owner of a small manufacturing business.

The client is selling his factory building and is not sure whether he will sell the business or just liquidate his assets. He asked the appraiser to provide him with an opinion of what all the machinery and equipment would be worth if sold. The appraiser provides the client with a brief letter on his stationery stating that the machinery and equipment is worth, in the appraiser's opinion, about \$7,000.

Three days later, the factory burned, and the machinery and equipment were destroyed. The owner submitted a claim for his machinery and equipment in the amount of the insurance of \$65,000. The insurance company investigator obtains a copy of the appraiser's letter stating the machinery and equipment was worth \$7,000.

Has the appraiser violated any part of USPAP? Does his letter constitute an appraisal report?

Response

Appraisers have a serious responsibility to affirm that accepting an assignment will result in credible assignment results, which are communicated in a manner that is not misleading.

In this example, the following Standards Rules appear to have been violated:

Standards Rule 7-1(c): Not render an appraisal in a careless or negligent manner

Standards Rule 8-1(a): Clearly and accurately set forth the appraisal in a manner that will not be misleading

Standards Rule 8-2: Various, including stating the identity of the client, intended users, intended use, property interest appraised, purpose of appraisal, scope of work, etc.

Standards Rule 8-2: Report type (not stated)

Standards Rule 8-3: Certification (not provided)

Note that a letter and an oral report both constitute appraisal reports. The appraiser's workfile must also contain all appropriate documentation and, in the case of an oral report, a certification that is both signed *and* dated (see **Record Keeping** section of the **ETHICS RULE** for a complete list of requirements).

Example C

An appraiser of personal property received a call from a business agent of a well-known country and western singer who had recently died. He was asked to undertake an appraisal of a collection of guitars for use in an estate tax matter. The appraiser was given the date of death. A formal proposal was written outlining the scope of work and the amount of the fee and was signed by the agent.

The appraiser had experience with appraising musical instruments owned by various "big name performers" that had been sold as collector items. He had also kept abreast of the market by subscribing to publications and maintaining contacts with dealers and collectors.

Research of the market revealed data to support the value of vintage guitars, but there were no sales, either private or through auctions, of any instruments owned by the deceased singer. He arrived at his value opinion and delivered the report to the agent along with his fee statement. The agent argued that the values were too low and, based on the stature of the deceased singer, they should be worth "thousands and thousands more"; the appraiser replied that he had found no sales to substantiate the agent's claim.

The agent was unhappy and insisted the appraiser change his appraisal—the appraiser would not. Did the appraiser comply with USPAP?

Response

In this case, the appraiser diligently researched the market for similar sales as well as the sales history of the subject property and any other guitars the deceased may have sold. Therefore, based on the information in the example, the appraiser appears to have been in compliance with USPAP, including both the **ETHICS and COMPETENCY RULES**.

Example D

The owner and operator of an antique shop advertises that she offers appraisal services. An attorney has asked her to perform an appraisal of personal property for estate taxes, explaining that the estate was left to an only son. She accepts the assignment.

After inspecting the furniture, glass, china, silver, and other household contents, the appraiser completed the appraisal. In the report, she provided a short cover letter that simply stated she had performed the appraisal, identified the total marketable cash value, made an offer to buy the estate at the value given, and included her signature. Attached were 13 pages of inventory with short descriptions and individual values for each property.

Did the appraiser comply with USPAP?

Response

No. The appraiser failed to comply with **STANDARDS 7 and 8** by not properly addressing the purpose and intended use of the appraisal. The value was not defined, nor was the approach to value (**Standards Rules 7-2 and 7-4**). The appraisal did not contain much of the information required by **Standards Rule 8-2(a) or (b)**, such as no limiting conditions, and no description or summary of the scope of work undertaken to complete the assignment. The report did not include a signed certification. (**Standards Rule 8-3**).

The appraiser did not comply with the **Conduct** section of the **ETHICS RULE**, which states: *An appraiser must perform assignments with impartiality, objectivity, and independence, and without accommodation of personal interests.* An offer to buy evidences a “prospective interest” in the subject of the assignment and implies, at least, a preference or inclination that precludes an appraiser’s impartiality.

The appraiser demonstrated a lack of knowledge by either education or experience that seriously affected both her development of an appraisal and her communication of the results in the report. Reference is made to the **ETHICS RULE**.

END OF  SECTION

Suggested Responses to Discussion Examples Section H—STANDARDS 9 and 10

Example A

An appraiser who is employed by a large accounting firm has been asked by an audit partner for a value based only on rules of thumb used in a specific industry. The audit partner intends to rely on the value as a “guideline valuation” for a buy-sell agreement. What should the appraiser do?

Response

Whether one calls an appraisal a *guideline* or a *rule of thumb valuation*, it is still an appraisal and must meet the requirements of USPAP. The appraiser should explain that he or she must perform every appraisal to meet certain minimum standards.

Example B

A senior associate at an appraisal firm was talking to a client about a recently prepared appraisal report. After reviewing the report, the client remarked that the “legal mumbo jumbo” in the certification appeared to be unnecessary given that he is a non-lawyer and he is likely to be the only one who would ever read the report anyway. He said that all of the qualifications and representations on this page meant nothing to him and that he preferred that the language be dropped from the report altogether. The appraiser wants to satisfy the client if at all possible, but he is unsure whether the certification is optional or not. What should he do?

Response

The certification is not optional and must contain language similar to that used in the Standards Rule. As stated in **Standards Rule 10-3**, it is a binding requirement from which departure is not permitted.

Example C

A company had recently redeemed a retired director’s stock. However, no mention of any prior transaction in company stock is made in a later appraisal. You are reviewing the appraisal and wonder why no mention of the prior transaction was made, especially since the prior transaction was conducted at a price more than double the appraisal conclusion. Upon further analysis, you find that the prior transaction seems to be overpriced and the appraisal results seem appropriate. Does the appraisal comply with USPAP?

Response

This issue is addressed in **Standards Rule 9-4(b)(iv)**, which calls for analyzing past sales of capital stock or other ownership interests in the business being appraised when they are relevant. The transaction appears relevant and thus should have been noted in the report; and, if it was not believed to be indicative of market value, this should have been discussed and supported.

Example D

In a highly competitive market, your client asks you to perform an appraisal. The intended use is to set the acquisition price of a competitor. The competitor is reluctant to give you the information you require, as confidentiality agreements are in place. Furthermore, the competitor is concerned that your client may not actually make the acquisition and would end up getting valuable insights into the competitor's operations. You do not believe you have adequate information to complete the assignment. Your client says that is all the information you will get and they need your analysis to make an offer. What should you do?

Response

The primary focus of this issue is the scope of work decision. The appraiser must determine whether he or she has enough information to reach a credible opinion of value and to present an appraisal report that, because of limited information available, is not misleading. If this is the case, the appraiser must also advise the client of the effects of the limitation, include such facts in the report, and gain assurance from the client that the performance of the appraisal as it is would be appropriate given the intended use.

Example E

An appraiser has had two years of experience as a business valuer. He has had no experience in appraising tangible assets such as real estate or fixtures and equipment, but has never had a problem as he assigns out that work when he feels it is needed.

In this case, he is appraising 100% of a company that owns and operates three outdoor movie theaters. They are marginally profitable and he develops a rather low value for the chain. He accepted the book value of the equipment and, although the real estate was owned, he did not get appraisals. However, he clearly stated in his report that he assumed a market value rent for the facility according to usual appraisal procedures.

The client sold the company with the three theaters. The new buyer promptly sold off the equipment at an auction, filed for permits, and, six months later, sold the land to a developer for five times the amount for which the appraiser had appraised the entire company and its assets. Has the appraiser performed within USPAP?

Response

The appraiser violated the requirement of **STANDARD 9** to consider and use all proper methods. He should have considered the value of the assets in liquidation. See **Standards Rule 9-3**. In addition, he violated the **COMPETENCY RULE**, since he should have been aware of the possible importance of the tangible assets and should have gotten the help of tangible asset appraisers to determine their value in exchange.

Example F

A senior appraiser with five years of appraisal experience has been working with a firm partner with 12 years of experience on a business appraisal for estate tax purposes. The appraiser has reached a preliminary opinion of value. Having performed most of the analysis, he presents it to the partner who agrees that the appraisal is well supported and reasonable. They call the client to report their results.

The client is shocked at how high the value is and says, “It will never do!” The partner quickly offers to re-examine the analysis and get back to him. When they hang up, the partner looks over the work papers for five minutes and instructs the appraiser to change them and the report, to use only the method that gave the lowest value, and to ignore certain issues the appraiser believes to be important.

They discuss these issues for some time. The appraiser does not believe the altered value is reasonable. The partner angrily insists that the appraiser change the report. The appraiser does so, but removes his name from it. What USPAP issues are presented in this situation?

Response

The partner violated the requirement of **Standards Rule 9-1** to *correctly employ those recognized methods and procedures that are necessary to produce a credible appraisal*. He also issued a report that was misleading. (See **Standards Rule 10-1**.) Additionally, according to **Standards Rule 10-3**, all individuals who provided significant professional assistance in an engagement are to sign or be named in the certification. Deleting the name of the person who did most of the analysis is not ethical and does not meet this Standards Rule.

END OF  SECTION