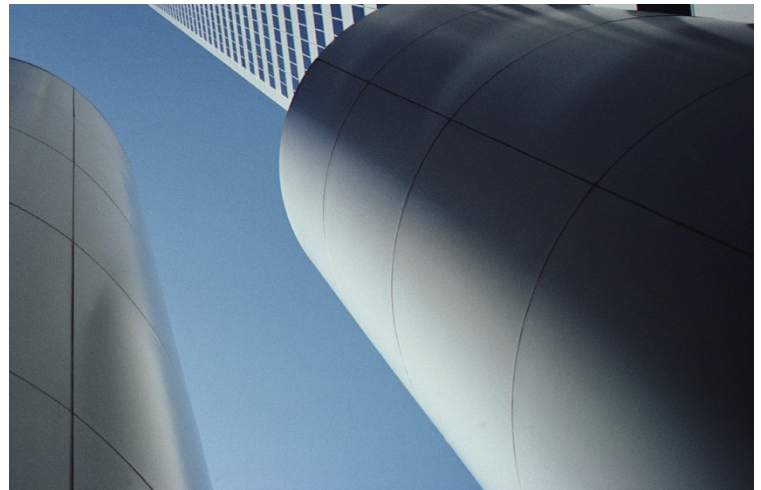


# Guide Note 13

## Performing Evaluations of Real Property Collateral for Lenders



### Introduction

Federally insured lending institutions in the United States are subject to regulations regarding real estate appraisals. For lending transactions involving real estate, a lender must obtain an appraisal from a state licensed or certified appraiser. There are twelve exemptions from this requirement. For three of these twelve exemptions, in lieu of an appraisal by a licensed/certified appraiser, the lender may obtain an *evaluation*.

An *evaluation* provides a market value of the real estate collateral. The preparer must be appropriately qualified and sufficiently independent from the transaction, but need not be a state licensed or certified appraiser. Even so, appraisers are often called upon to provide them.

How can an appraiser prepare an evaluation for a lender and comply with the Standards of Valuation Practice (SVP) or Uniform Standards of Professional Appraisal Practice (USPAP)?

# GUIDE NOTE 13

## Basis for Proper Practice

The Interagency Appraisal and Evaluation Guidelines <https://www.fdic.gov/news/news/financial/2010/fil10082a.pdf> issued by the federal agencies<sup>2</sup> in December 2010 provide full details about when appraisals and evaluations are required, who can provide them, and how they must be performed. Section V (pp. 3-5) addresses the independence requirements for both appraisals and evaluations. Section VI (pp. 5-6) addresses the selection, evaluation and monitoring the performance of those providing these services. Section XI (pp. 11-12) addresses when evaluations are required. Section XII (pp. 12-13) addresses the development process for an evaluation, and Section XIII (pp. 13-14) addresses the required content of an evaluation report. Section XV (pp. 15-18) addresses the review of appraisal and evaluation reports.

Portions of SVP that are relevant to this topic include the Definitions section, and STANDARDS A and C; relevant portions of USPAP include the DEFINITIONS section, the SCOPE OF WORK RULE, and STANDARDS 1 and 2.

The definitions sections establish the application of certain terminology in SVP and USPAP. See especially the definitions of *appraisal* and *report*.

Standards Rules A-2 and A-3 in the SVP and the USPAP SCOPE OF WORK RULE presents obligations related to problem identification, research and analyses.

SVP STANDARDS A and C and USPAP STANDARDS 1 and 2 establish requirements for the development and communication of a real property appraisal.

## What is an Evaluation?

An *evaluation* is defined in the Guidelines as “A valuation permitted by the Agencies’ appraisal regulations for transactions that qualify for the appraisal threshold exemption, business loan exemption, or subsequent transaction exemption.”<sup>3</sup>

## When are Evaluations Used?

A lender may obtain an evaluation in lieu of an appraisal when the loan transaction:

- Has a transaction value equal to or less than \$500,000 (\$250,000 prior to April 9, 2018);
- Is a business loan with a transaction value equal to or less than the business loan threshold of \$1 million, and 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:
  - There has been no obvious and material change in 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
  - There is no advancement of new monies other than funds necessary to cover reasonable closing costs.<sup>4</sup>

## Who Can Prepare Evaluations?

According to the Guidelines, persons performing evaluations should be independent of the loan production and collection processes and have no direct, indirect or prospective interest, financial or otherwise, in the property or transaction. In addition, the Guidelines stipulate that an institution should have criteria for selecting, evaluating, and monitoring the performance of persons who perform evaluations. The criteria should ensure that:

- The person selected possesses the requisite education, expertise, and experience to competently complete the assignment.
- The work performed by persons providing evaluation services is periodically reviewed by the institution.

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<sup>1</sup> For the remaining 9 exemptions, the lender is not required to document the collateral value with either an evaluation or an appraisal from a state licensed or certified appraiser.

<sup>2</sup> These agencies include the Office of the Comptroller of the Currency, Treasury (OCC); the Office of Thrift Supervision (OTS); Board of Governors of the Federal Reserve

System (FRB); Federal Deposit Insurance Corporation (FDIC); and the National Credit Union Administration (NCUA).

<sup>3</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, p. 41.

<sup>4</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, p. 11.

- The person selected is capable of rendering an unbiased opinion.
- The person selected is independent and has no direct, indirect, or prospective interest, financial or otherwise, in the property or the transaction.
- Persons who perform evaluations should possess the appropriate appraisal or collateral valuation education, expertise, and experience relevant to the type of property being valued. Such persons may include appraisers, real estate lending professionals, agricultural extension agents, or foresters.<sup>5</sup>

Individuals who perform evaluations need not be state licensed or certified appraisers. However, state licensed and certified appraisers are not precluded from providing them. Because appraisers are independent and qualified to provide valuations of real property, they are often called upon to provide evaluations. Footnote to be inserted here: Appraisers are advised to check with the appraiser licensing agency in the state where the real property is located about state requirements concerning the performance of evaluations.

The Guidelines state that an institution should review evaluations (and appraisals) to ensure they comply with the Agencies' appraisal regulations and are consistent with supervisory policies and the institution's own internal policies. The review should ensure the evaluation contains sufficient information and analysis to support the decision to engage in the transaction.<sup>6</sup>

## What are the Development Requirements for Evaluations?

The Interagency Appraisal and Evaluation Guidelines establish parameters for the development of an evaluation.

An evaluation must:

- Be consistent with safe and sound banking practices;
- Support the institution's decision to engage in the transaction;<sup>7</sup>
- Provide a reliable estimate of the collateral's market value as of a stated effective date prior to the decision to enter into the transaction;
- Be based on a valuation method that is appropriate for a transaction rather than the method that renders the highest value, lowest cost, or fastest turnaround time;
- Address the property's actual physical condition and characteristics;
- Address the economic and market conditions that effect the estimate of the collateral's market value, and
- Not be based on unsupported assumptions, such as an assumption that the property is in average condition, the zoning will change, or the property is not affected by adverse market conditions.<sup>8</sup>

While the Guidelines do not state that a property inspection is necessary in all cases, they do say the institution should "establish criteria for determining the level and extent of research or inspection necessary to ascertain the property's actual physical condition, and the economic and market factors that should be considered in developing an evaluation." If a property inspection is not performed, "the institution should be able to demonstrate how these property and market factors were determined."<sup>9</sup>

The Guidelines further clarify that broker price opinions (BPOs), automated valuation models (AVMs), and tax assessment values (TAVs) do not suffice in themselves as evaluations. However, they can be used to assist in the development of an evaluation.<sup>10</sup>

## What are the Reporting Requirements for Evaluations?

According to the Guidelines:

An evaluation should contain sufficient information detailing the analysis, assumptions, and conclusions to support the credit decision. An evaluation's content should be documented in the credit file or reproducible. The evaluation should, at a minimum:

1. Identify the location of the property.
2. Provide a description of the property and its current and projected use.

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<sup>5</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, p. 5.

<sup>6</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, p. 16.

<sup>7</sup> This phrase has been erroneously interpreted to mean the evaluation must provide a predetermined conclusion. To the contrary, this statement means that if the evaluation does not support the decision to engage in the transaction, the lender should not pursue the transaction.

<sup>8</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, pp. 12-13.

<sup>9</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, p. 13.

<sup>10</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, pp. 32-35, 40.

3. Provide an estimate of the property's market value in its actual physical condition, use and zoning designation as of the effective date of the evaluation (that is, the date that the analysis was completed), with any limiting conditions.
4. Describe the method(s) the institution used to confirm the property's actual physical condition and the extent to which an inspection was performed.
5. Describe the analysis that was performed and the supporting information that was used in valuing the property.
6. Describe the supplemental information that was considered when using an analytical method or technological tool.
7. Indicate all source(s) of information used in the analysis, as applicable, to value the property, including:
  - a. External data sources (such as market sales databases and public tax and land records);
  - b. Property-specific data (such as previous sales data for the subject property, tax assessment data, and comparable sales information);
  - c. Evidence of a property inspection;
  - d. Photos of the property;
  - e. Description of the neighborhood; or
  - f. Local market conditions.
8. Include information on the preparer when an evaluation is performed by a person, such as the name and contact information, and signature (electronic or other legally permissible signature) of the preparer.<sup>11</sup>

## How Can an Appraiser Provide an Evaluation and Comply with Professional Valuation Standards?

SVP addresses the development of a real property appraisal in STANDARD A and the reporting of a real property appraisal in STANDARD C. USPAP addresses this development process in STANDARD 1 and the related reporting requirements in STANDARD 2. The problem identification and scope of work requirements in SVP and USPAP allows considerable flexibility in the development process. The scope of work for an assignment may be adjusted as appropriate for the intended use. The degree of property inspection, the extent of the data collection process, and the type and level of analysis can vary as needed, as long as the resulting opinions and conclusions are credible in light of the intended use. For purposes of preparing an evaluation pursuant to the Guidelines, consideration may be given to these factors.

For example, in some cases it may be possible to rely on a prior appraisal report for information about the property, such as its size and physical attributes. When this is done, the report must clearly state the source of the information, that it was assumed to be accurate, and that the value conclusion might be different otherwise.

In other cases, an "at least" conclusion might be all that is required. SVP and USPAP both permit a value conclusion to be stated as a single number, a range, or a relationship to some amount<sup>12</sup> – for example, "not more than," "not less than," or "at least" some benchmark amount. The benchmark amount could be a prior appraised value, sale price, or other amount that is relevant to the intended use.

Narrowing the scope of work could also mean omitting one or more of the three approaches to value. For example, if the sales comparison approach is the primary approach (as is often the case for single family residences and owner occupied commercial properties), it may be appropriate to omit the cost and income approaches. If the income approach is the primary approach (as is often the case for income-producing properties), it may be appropriate to omit the sales comparison and cost approaches. While all three approaches are generally helpful, not all three are critical to every valuation problem, given the intended use.

SVP presents the minimum requirements for reporting an appraiser's opinions and conclusions in appraisal and review assignments. Under USPAP, STANDARD 2, two reporting options are available for written appraisal reports. The minimal report option is the Restricted Appraisal Report. This option is permitted only when the client is the sole intended user of the report. A Restricted Appraisal Report is not required by USPAP to include the data and analyses used to arrive at the value opinion, or a detailed property description, though it can be supplemented to include that information. Because the Guidelines require this detail, a Restricted Appraisal Report that meets the *minimum* requirements of USPAP would not be sufficient to serve as an evaluation. A USPAP-compliant Restricted Appraisal Report that is supplemented to include all of the information required by the Guidelines should be sufficient.

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<sup>11</sup> Interagency Appraisal and Evaluation Guidelines, December 2010, pp. 13-14.

<sup>12</sup> SVP, definition of appraisal (lines 3-6), USPAP, DEFINITIONS. See [Comment](#) to the entry for *appraisal*.

The following are two outlines intended to assist in creating a report format to meet the minimum requirements of professional valuation standards as well as the Guidelines for an evaluation. Outline #1 is for use when the applicable valuations standards are the SVP, while Outline #2 is for use when the applicable valuation standards are USPAP. In each case, while additional elements may be added, none should be deleted, as deleting elements might cause the report to fail to meet the SVP or USPAP reporting requirements and/or the requirements of the Guidelines for an evaluation. Note that editing is required for the italicized items.

# OUTLINE #1 FOR AN EVALUATION

(SVP and Interagency Appraisal and Evaluation Guidelines)

DATE OF REPORT: DD/MM/YYYY

CLIENT: *Lender ABC.*

INTENDED USER(s): For the sole use of *Lender ABC.* This report is not intended for use by other parties.

INTENDED USE: To assist the client in establishing collateral value in a lending transaction that requires an "evaluation" as set forth in the Interagency Appraisal and Evaluation Guidelines. This report is not intended for any other use.

TYPE OF VALUE AND SOURCE: *State the type of value and cite the source of its definition.*

EFFECTIVE DATE OF VALUE OPINION: DD/MM/YYYY

REAL PROPERTY INTEREST VALUED: *FEE SIMPLE/LEASED FEE/LEASEHOLD/OTHER*

IDENTIFICATION OF REAL ESTATE: 100 MAIN ST., CITY, STATE

SPECIAL ASSUMPTIONS: Clearly state any special assumption(s) on which the analysis is premised and state that the use of the special assumption might have affected the value conclusion.

SCOPE OF WORK: In preparing this analysis, I:

- *Describe level of inspection. Include the date of property inspection, if applicable.*
- *Describe process of gathering information on comparable land and improved sales, rents operating expenses, construction costs, accrued depreciation, capitalization and/or yield rates.*
- *Describe how comparable sales and/or rental information was confirmed.*
- *Describe valuation approaches used and address the exclusion of any of the typical approaches (sales comparison, cost, income).*

LOCATION DESCRIPTION: *Describe the property's location and discuss local market conditions.*

PROPERTY DESCRIPTION: *Provide a description of the property and its current and projected use. Discuss the property's physical condition. Attach photographs.*

VALUATION ANALYSIS: *Describe the analysis that was performed (approaches) and the supporting information that was used in valuing the property. For example, if a sales comparison approach was performed, include an adjustment grid showing comparable analysis. If an income approach was performed, show development of income and expense estimates, capitalization rate and/or discount rate. Include sources of comparable sales information. Include external data sources (such as market sales databases and public tax and land records).*

VALUE CONCLUSION: \$XXX,XXX

CERTIFICATION: I certify that, to the best of my knowledge and belief:

- The reported analyses, opinions and conclusions were developed, and this report complies with the requirements of the Code of Professional Ethics, Standards of Professional Practice, and the Standards of Valuation Practice of the Appraisal Institute.
- I have no (or the specified) present or prospective interest in the property that is a subject of this engagement and no (or the specified) personal interest with respect to the parties involved.
- No one provided significant real property appraisal assistance to the person signing this certification. *(If there are exceptions, the name of each individual providing significant real property appraisal assistance must be stated.)*
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- (Designated Members only) As of the date of this report, I have/have not completed the continuing education program for Designated Members of the Appraisal Institute.
- (Candidates only) As of the date of this report, I have/have not completed the Standards and Ethics Education Requirements for Candidates of the Appraisal Institute.
- (Practicing Affiliates only) As of the date of this report, I have/have not completed the continuing education program of the Appraisal Institute for Candidates of the Appraisal Institute.

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Signature

# OUTLINE #2 FOR AN EVALUATION

(USPAP and Interagency Appraisal and Evaluation Guidelines)

DATE OF REPORT: DD/MM/YYYY

CLIENT/INTENDED USER: For the sole use of *Lender ABC*. This report is not intended for use by other parties.

INTENDED USE: To assist the client in establishing collateral value in a lending transaction that requires an "evaluation" as set forth in the Interagency Appraisal and Evaluation Guidelines. This report is not intended for any other use.

ASSIGNMENT OBJECTIVE: To develop an opinion of the Market Value, as defined by the federal financial institution regulatory agencies, of the stated interest in the subject property.

TYPE OF VALUE AND SOURCE: *State the type of value and cite the source of its definition.*

EFFECTIVE DATE OF VALUE OPINION: DD/MM/YYYY

REAL PROPERTY INTEREST VALUED: *FEE SIMPLE/LEASED FEE/LEASEHOLD/OTHER*

IDENTIFICATION OF REAL ESTATE: 100 MAIN ST., CITY, STATE

CURRENT LISTING/CONTRACT INFORMATION: The subject property is/is not currently listed/under contract for \$XXX,XXX. This asking/contract price is/is not consistent with the appraiser's opinion of market value. (If not consistent, explain discrepancy.)

PREVIOUS SALE DATA: Include data and analysis of any transaction within the last 3 years involving the subject property.

ASSIGNMENT CONDITIONS: Clearly state any extraordinary assumption(s) on which the analysis is premised and state that the use of the extraordinary assumption might have affected the assignment results.

SCOPE OF WORK: In preparing this analysis, I:

- *Describe level of inspection. Include the date of property inspection, if applicable.*
- *Describe process of gathering information on comparable land and improved sales, rents operating expenses, construction costs, accrued depreciation, capitalization and/or yield rates.*
- *Describe how comparable sales and/or rental information was confirmed.*
- *Describe valuation approaches used and address the exclusion of any of the typical approaches (sales comparison, cost, income).*

REPORT OPTION: This report is a Restricted Appraisal Report in accordance with Standards Rule 2-2(b) of the Uniform Standards of Professional Appraisal Practice and is intended to meet the requirements for an "evaluation" according to the Interagency Appraisal and Evaluation Guidelines. Additional supporting documentation is retained in the appraiser's workfile. The development of the appraiser's opinions and conclusions set forth in this report might not be understood properly without additional information in the appraiser's workfile. However, in order to meet the requirements for an "evaluation" according to the Interagency Appraisal and Evaluation Guidelines, this report has been supplemented with additional information about the subject property and its market, as well as the data, reasoning, and analyses that were used in the valuation process.

LOCATION DESCRIPTION: *Describe the property's location and discuss local market conditions.*

PROPERTY DESCRIPTION: *Provide a description of the property and its current and projected use. Discuss the property's physical condition. Attach photographs.*

HIGHEST AND BEST USE CONCLUSION: Current use/other (if other, describe).

VALUATION ANALYSIS: Describe the analysis that was performed (approaches) and the supporting information that was used in valuing the property. For example, if a sales comparison approach was performed, include an adjustment grid showing comparable analysis. If an income approach was performed, show development of income and expense estimates, capitalization rate and/or discount rate. Include sources of comparable sales information. Include external data sources (such as market sales databases and public tax and land records).

VALUE CONCLUSION: \$XXX,XXX

ESTIMATED EXPOSURE TIME: (amount of time the subject property would have been on the market to bring a sale as of the effective date of the value opinion): XXXX

CERTIFICATION:

I certify that, to the best of my knowledge and belief:

- The statements of fact contained in this report are true and correct.
- The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions and are my personal, impartial, and unbiased professional analyses, opinions, and conclusions.
- I have *no (or the specified)* present or prospective interest in the property that is the subject of this report and *no (or the specified)* personal interest with respect to the parties involved.
- I have performed *no (or the specified)* services, as an appraiser or in any other capacity, regarding the property that is the subject of this report within the three-year period immediately preceding acceptance of this assignment.
- I have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
- My engagement in this assignment was not contingent upon developing or reporting predetermined results.
- My compensation for completing this assignment is not contingent upon the development or reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value opinion, the attainment of a stipulated result, or the occurrence of a subsequent event directly related to the intended use of this appraisal.
- My analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the Uniform Standards of Professional Appraisal Practice.
- I have *(or have not)* made a personal inspection of the property that is the subject of this report. *(If more than one person signs this certification, the certification must clearly specify which individuals did and which individuals did not make a personal inspection of the appraised property.)*
- No one provided significant real property appraisal assistance to the person signing this certification. *(If there are exceptions, the name of each individual providing significant real property appraisal assistance must be stated.)*
- The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the Code of Professional Ethics and Standards of Professional Practice of the Appraisal Institute.
- The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.
- *(Designated Members Only)* As of the date of this report, I have/have not completed the continuing education program for Designated Members of the Appraisal Institute.
- *(Candidates Only)* As of the date of this report, I have/have not completed the Standards and Ethics Education Requirement of the Appraisal Institute for Candidates.
- *(Practicing Affiliates Only)* As of the date of this report, I have/have not completed the continuing education program of the Appraisal Institute for Practicing Affiliates.

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Signature



# Summary of Standard Practices

1. “Evaluations” per the Interagency Appraisal and Evaluation Guidelines are market value opinions that may be provided by individuals who are not state licensed or certified appraisers. However, state licensed and certified appraisers may provide them.
2. The Interagency Appraisal and Evaluation Guidelines set forth development and reporting requirements for “evaluations.” The reporting requirements do not exactly align with the reporting requirements for an appraisal under SVP or USPAP. However, an appraiser subject to SVP or USPAP can prepare an “evaluation” that meets both the Guidelines and SVP or USPAP.
3. SVP and USPAP allow an appraiser to adjust the scope of work for a valuation assignment as long as the resultant value opinion is credible, given the intended use. When preparing an “evaluation” the appraiser may consider narrowing the scope of work as appropriate.

(Please Note: The purpose of the Guide Notes to the Standards of Professional Practice is to provide Appraisal Institute Designated Members, Candidates, and Practicing Affiliates with guidance as to how the requirements of the Standards may apply in specific situations.)

Effective October 31, 2012  
Minor revisions 2017, 2018