



ARIZONA BOARD OF APPRAISAL

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Newsletter RE: Comp Checks/Cost Approach

December 14, 2010

COMP CHECKS:

Yesterday, on my previous appraiser email address, I received a solicitation as an appraiser. This email solicitation for appraisers is currently going around and asks appraisers to sign up to do Comp Checks for a fee that require no signature, invoicing, photos, on-site inspections or sign-up fees but you must be a licensed or certified appraiser. There are *very fine* lines as to how you can do this without being required to comply with USPAP Standards 1 and 2.

The solicitation specifically advertises that loan officers across the nation are using these comp checks to *"determine true value before arbitrarily denying a loan application based on poor AVM's and other faulty valuation models that contain many errors like Zillow"* (direct quote from the email) Does the language *"determine true value"* sound like an appraisal? There may be more to the story but that is the information stated in the email.

In any event, Appraisers should be aware of and understand 2010 USPAP FAQ 35-page F16; FAQ 177-page F82; and FAQ 176-page F81 before moving forward. Please refer to USPAP. As you probably know, USPAP together with FAQs and Advisory Opinions are also on line and you can download the FAQ pdf which will make it searchable and easier to use on your computer.

COST APPROACH:

One of the most often heard issues in front of the Board is the cost approach. While the use of the cost approach is not always required by the client, it must be considered and if relevant completed per USPAP. There have been numerous cases heard by the Board that were a result of a complaint filed for reasons other than the cost approach but when reviewed and discussed by the Board the cost approach was noted to be flawed. Most deficiencies include lack of data or explanation regarding opinion of site value, references to outdated sources, the lack of use or understanding of functional and external obsolescence, and cost figures that are not credible. All are included on the "most often seen" list.

The cost approach can be a great test of reasonableness. If both the cost and sales comparison approaches have been completed effectively and there is a disparity between the opinion of value from the two approaches the difference will likely fall into functional or external obsolescence. Ultimately the cost approach, including functional and external depreciation/obsolescence should tend to mirror the sales comparison approach. The Board has seen many appraisals that may have a sales comparison

approach indicating, say \$200,000 and a cost approach which may indicate \$300,000 or more. In our current market the difference is likely external obsolescence due to recent and previous well known market conditions but functional obsolescence is also very common and there may be a combination of both. Disparity such as this example may indicate that the appraiser does not understand the cost approach and at a minimum will generate questions by the Board.

If you are not including functional or external obsolescence in your cost approach you may want to do some research. *The Appraisal of Real Estate Thirteenth Edition*, published by the *Appraisal Institute* has an excellent chapter on The Cost Approach starting on page 377. This chapter includes the definition and further explanation of the three major components of depreciation starting on page 391. There are other publications and sources from which to draw this information. Use Google, check with some of the professional organizations, contact the educators, develop a relationship with peer appraisers that you can discuss these issues with. If you are in a cost approach class don't hesitate to ask the instructor to go into detail about depreciation because the Board is probably going to ask if they are reviewing one of your reports. It is methodology that you need to be familiar with. It can not only be a useful test for reasonableness in your daily work but the proper understanding and use of the cost approach will add credibility to you as the appraiser.

Be pro-active. Try to identify areas you think you may be weak in or don't feel as confident about as you would like and seek out the information you need either to confirm your knowledge or increase your knowledge. Don't wait to hear about it in a class or have the Board ask you about it. An educated and competent appraiser creates inner confidence and credibility for his or her self and the entire profession.

By the way, try to attend one of the Board meetings. Attending a Board meeting not only provides insight as to how the Board functions but will alert you to current issues that the Board is hearing. The next Board meeting is this Thursday, December 16, 2010, 9 am at the West Tower Capital building. The address is 1700 W. Washington but your GPS will put you on the wrong side of the complex. Go to 19th Avenue and Washington. The NE corner is an open free parking lot that is accessed from either 19th Ave or Washington. At that point you will see the West Tower to the east. Go in the front, pass security, (no TSA pat downs here), take the elevators to the right, get off at the 3rd floor and you will be directly in front of the hearing room. We'll see you there.

If we don't communicate till then, on behalf of the Board and the Board staff we wish you all a Merry Christmas, Happy Holidays, or your Season of Choice and may you celebrate your Season in safety.

Sincerely,

A handwritten signature in blue ink that reads "Dan Pietropaulo". The signature is fluid and cursive, with the first name "Dan" being the most prominent.

Dan Pietropaulo #30412
Executive Director
Arizona Board of Appraisal

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