

Should Appraisers Guarantee Rebuilds?

by John Lifflander, ASA

FOR YEARS, LENDERS HAVE BEEN ACCUSTOMED TO ASKING RESIDENTIAL APPRAISERS IF A HOME CAN BE REBUILT OR NOT. NORMALLY, THIS QUESTION ARISES WHEN THE HOME IS IN AN ATYPICAL ZONE, SUCH AS A COMMERCIAL ZONE, THAT MAY NOT NORMALLY ALLOW FOR RESIDENTIAL USES. The lender is concerned that if the property is destroyed – via fire, flood or some other way – there will be a loss if rebuilding is prohibited. Sometimes the appraiser is asked to make a statement that the home can be rebuilt, and other times the appraiser is asked to procure a “rebuild letter” from the local government office that has that authority.

However, when an appraiser attempts to guarantee the rebuilding of a property, he or she takes on substantial liability that may lead to troublesome litigation.

Could this happen to you?

For example, an appraiser completes an assignment on a single-family residence built many years before the zoning changed from single-family residential to multifamily residential. The lender is concerned about whether or not the property can be rebuilt, because often multifamily zoning does not allow single-family residences. The lender contacts the appraiser and requests that she determine if the property can be rebuilt or not and send an addendum regarding this matter. The company she works for tells her to call the county and get the information. The appraiser calls the planning department and a man named Joe tells her that the house “should be rebuildable, no problem.” The appraiser then writes an addendum stating that the home is rebuildable.

One year after the loan is made, the subject area floods, even though it is not in a mapped flood zone. There is no flood insurance on the property, and the building becomes a total loss. The owner leaves the property and stops paying the mortgage, and the lender forecloses due to failure of payment. The lender finds out that only a multifamily residence can be rebuilt on the property, and the lender attempts to sell the land for this use. However, in order to build a multifamily structure, the building department requires that a new, larger sewer line be installed and concrete sidewalk be poured. Because the lot is small, it is not cost-effective

to pay for all of this infrastructure work, and the lot stays on the market for a long time. The lender keeps lowering the price, and finally the lot sells for a very low amount – much lower than the appraiser valued the land at, even though prices have risen in the past year.

The lender hires a different appraiser to determine what the sale price might have been if the zoning had allowed for the single-family residence to be rebuilt. Under those circumstances, the sewer enlargement and the addition of sidewalks would not have been necessary. The differential in value is \$50,000. The lender then sues the first appraiser for this amount of money, plus court costs and attorney fees, the recovery of which is allowed in the state.

The original appraiser calls the planning department and tries to find the man who assured her that the residence could be rebuilt. She only has his first name, and the manager tells her no one by that name works there any more. Regardless, he says, no one in that department would ever say anything about rebuilding a property, because planning does not deal with such issues. He tells her that she should have spoken with the building department regarding this matter. The appraiser finally does track Joe down, but he says he does not remember speaking to her, adding that he never would have commented about rebuilding because that was not part of his job.

The appraiser is then subjected to a series of unfortunate occurrences: the lingering litigation, which takes almost two years; she is cancelled by the errors and omissions insur-

ance company that her employer had covering her; and, to bolster their case, the lender files a complaint against her with the state appraisal board claiming she has been negligent and incompetent. Next, her employer dismisses her because a new insurance carrier cannot be found for her, and the company wants to be as separated as possible from the problem. When she reminds them that they had told her to give out this information, they say she should have researched the information more carefully.

How to avoid a similar problem

The appraiser was simply trying to satisfy the request of the lender. She called the government office and got the answer that she thought was correct. However, although she tried to do things properly, she made several mistakes.

First, she agreed to perform a service that she had not actually been trained to do. The lender hired her to value the property, but she agreed to guarantee something that she not only lacked the expertise to guarantee, but which was actually beyond the scope of the work she was hired to perform.

Secondly, she did not think about the liability of her statement regarding this property. This is quite understandable since the appraisal office she worked for made the same mistake by routinely agreeing to get this type of information for lenders. They also asked their appraisers to fulfill these requests without training them on specific procedures to accomplish the task, and without consideration of the potential legal ramifications they

See REBUILDS, page 48

REBUILDS, continued from page 32

were incurring for providing this free service.

Appraisers need to realize that when they make a statement about rebuilding a property, they have just become liable if it turns out that it cannot be rebuilt exactly as it exists at the time of the appraisal. Even if a property is in a residential zone, it may have many new requirements, such as different setbacks, height requirements or building material requirements, if the property must be reconstructed.

Getting a “Rebuild Letter”

Some lenders ask the appraiser to get a “rebuild letter.” While a letter of this sort does provide more assurance that the property can be rebuilt than does a casual conversation with some government employee, there are compelling reasons against making this part of your service portfolio. In some instances there is a charge for such letters and in others they may only be issued to the homeowner.

In any event, getting such a letter often takes a considerable amount of time, and appraisers need to determine if this is an activity that they truly want to make as part of their offered services. If it is, it may be that an extra fee should be charged for it. It is also recommended that it should be supplied to the lender with a disclaimer regarding any liability on the appraiser’s part, in case there are new requirements that the letter does not address. For example:

The subject property is zoned R-5000, single-family residential. This zoning normally allows rebuilding for a residential property with a minimum of 5,000 square feet. However, the appraiser does not guarantee that this specific property can be rebuilt.

Appraisers are also advised to use such a statement only when it is requested; otherwise, no statement regarding this issue should be written into the appraisal.

Appraisers might also consider drafting a standard statement in response to requests for a confirmation of rebuilding that explains the appraiser does not wish to become liable in this matter. Lenders know appraisers live in a very litigious environment and should not press on this issue. Risking litigation that is easily avoidable is foolhardy. Remember, when a property is foreclosed upon, and the appraisal is examined with a “fine-tooth comb,” everything the appraiser says can and will be used against him or her. ■

John Lifflander, ASA, is a Certified General Appraiser who owns Covenant Consultants, Inc., an appraisal company in Vancouver, Wash. He is a former administrative law judge for property tax valuation issues for the state of Oregon. Please note: this article should not be construed as legal advice or a legal opinion on any specific set of circumstances. The reader is urged to consult a lawyer regarding any specific legal questions on this matter.

PRESIDENT, continued from page 2

chance to trade tips and techniques to make maximum use of the service. It’s accessible even if you aren’t yet using STDB to find out more about its features from those who are.

If networking on an international scale is more your cup of tea, this fall valuers from throughout the Pacific Rim as well as the United States and Canada will attend the 23rd Pan Pacific Congress being hosted by the Appraisal Institute in

San Francisco. The Appraisal Institute was one of the founding members of this biennial event, and now more than ever, we can all benefit from the insights of fellow valuers from throughout the Pacific Rim. One has only to look at how the markets in China and India are continuing to grow to recognize that those economies in particular will exert greater and greater influence on global real estate markets. We anticipate

that the Congress will provide a unique view of this growth and its effect on our economy and markets (see page 36 for more information).

Networking plays a powerful – if sometimes unrecognized – role in our professional lives. The Appraisal Institute seeks to provide outlets and opportunities for such networking. It’s all part of our efforts to “create value through service.” ■