



UNIT 7

APPRAISALS AND HOME VALUE APPRECIATION

The purchase of a home is the largest investment that the typical person ever makes. Unlike the purchase of a new car or truck that becomes less valuable over time, a home typically appreciates, or goes up, in value. A home also provides the “service” of shelter, so homeowners get the best of both worlds—they get to use a product that becomes more valuable as time goes on.

The **value** of something, according to the economist, is the worth of something in dollars and cents as determined by the market. The value of many products—a gallon of gas for example—is relatively easy to establish because the market is so large and because there are so many buyers and sellers. However, the value of any given home is much more difficult to establish for several reasons: it is not likely to be identical to other homes in the community; it typically comes on the market infrequently; and, it is a big-ticket item which limits the number of potential buyers. As a result, we don’t always know what a particular home, property, or building is actually worth.

This is where the appraiser comes in, because the **appraiser** is a real estate professional who tries to determine the market value of property when a true market value is not available. The process of determining and assigning the value is the **appraisal**, and the appraisal has many uses. A lender, for example, usually wants to see an appraisal before a loan is made; an insurance company may want an appraisal before a policy is issued, and a homeowner may want an appraisal to find the approximate value of a home before it is listed for sale.

Student Learning Objectives:

- Students will learn about the role of appraisers and appraisals in the real estate industry.
- Students will examine several techniques used by appraisers to determine value.

Key Concepts:

value

appraiser

appraisal

LESSON 7-1: THE APPRAISER IN YOUR COMMUNITY

The appraiser has a unique role in the real estate community because, unlike the broker or the realtor, the appraiser's compensation is not based on the value of the property. Instead, the appraiser usually charges a flat fee that will amount to several hundred dollars or more, based on the complexity of the property. This gives the appraiser a certain objectivity because the appraiser has no vested interest in the dollar value of the appraisal.

In the end, the objectivity, skill, and impartiality of the appraiser are his or her greatest assets because real estate appraising is an art, not a science. All states require that appraisers be licensed or certified, but the requirements vary widely from state to state. As a result, the purpose of the first activity is to find out more about the educational, licensing, and professional qualifications of the real estate appraiser in your community. While the results will vary from one state to another, most students will be surprised to discover the degree of professionalism that most appraisers have for their vocation.

Materials Needed:

- One copy of *Activity Sheet 7-1: The Appraiser in Your Community* for each student.

NOTE: If you do not elect to use this activity as a take-home assignment, you will need to invite a real estate appraiser to your class in order to complete this activity.

Teaching the Lesson:

1. Laws and regulations regarding the work of real estate appraisers varies from state to state, although there has been a gradual movement toward uniform standards and practices. Accordingly, the best way to find out about the educational, licensing, and other requirements regarding real estate appraisers in your community is to ask an expert – the real estate appraiser in your community.
2. Tell the students that they are going to engage in some original research that will give them more information about the real estate appraisal industry and/or practices in their community. The information they discover will be shared with the class in a manner of your choosing (*an oral report, a class discussion, or a short one-page essay, depending on the skills of the students and/or your own pedagogical preferences*).
3. Distribute a copy of *Activity Sheet 7-1: The Appraiser in Your Community* to each student. Note that the questions on the sheet are not inclusive, and that they must provide two more of their own unique questions. Assign a time for completion and let the student begin.

Debriefing the Lesson

This is an open-ended assignment, so encourage the students to be as creative as possible with regard to the questions they ask. Questions such as “What do you like best about your job?” or “What do you like least about your job?” usually invoke a particularly wide range of interesting responses.

Remember that there are no correct answers for this activity as requirements for the profession vary considerably from state to state. Encourage your students to have fun, and encourage them to learn as much as possible.

LESSON 7-2: TECHNIQUES OF REAL ESTATE APPRAISING

The process of conducting a real estate appraisal is more complicated than most people realize and has been the subject of many long and comprehensive texts. As a result, the purpose of this activity is only to give students an idea of some of the techniques used. A realistic appraisal is best left to the experts.

The main thing to keep in mind is that the appraiser is trying to estimate the value of a property if it were to be sold in an open and competitive market. Sometimes the price is relatively easy to determine, as when a house is put up for sale in a subdivision of similar homes, some of which may have been recently sold. At other times the process is much more complex. A city, for example, might want to purchase a strip of land in a rural or outlying area in order to put in a highway or sewer system. If the property was never offered for sale by the owner, and if near-by properties are not up for sale, then the process of estimating value is much more difficult.

Materials Needed:

- Provide at least one copy of *Activity Sheet 7-2: Techniques of Real Estate Appraising* for each student.

NOTE: This activity requires a wrap-up visit with a real estate appraiser. Review the activity below before you assign the activity sheets, and schedule a class visit with an appraiser so that you can effectively debrief the activity.

Teaching the Lesson:

1. Real estate valuations are frequently based on three classic approaches to value: the *sales comparison*, *cost*, and *income approaches*. Each has their strengths, and appraisers will frequently

apply all three approaches and then base their final recommendation on an average (or weighted average) of the three methods.

- The **sales comparison** is a valuation based on the price of similar properties. For example, the value of one house in a subdivision may be largely determined by the prices people have paid for other houses in the vicinity. Real estate brokers often keep track of data like this to help their clients determine the listing price for their house. Some web site search engines like *Yahoo!* will even help you find the prices paid for other homes in your neighborhood. The difficulty, of course, is that not all homes are the same. One may be on a dead-end street while another nearer to a bus station or school bus stop, be closer to the interstate, have a better view, be in a different school district, or be of a different size. As difficult and subjective as this may be, all of these factors will drive the value of a particular property up or down.
- The **cost approach** assumes that the current value is in some way related to earlier costs that were expended to construct, purchase, improve, or otherwise upgrade the property. If the property being valued is so unique that a sales comparison is difficult—if not impossible—to obtain, then this method may be used. The value of a farm, for example, may be approximated by the cost of the property ten years ago, plus the cost of the buildings, road, and drainage improvements made since the purchase, plus some increment to allow for the appreciation of the land over time. While this is certainly an approximation, it is reasonable to assume that the seller wants to get his or her money back, plus a small amount of profit, whenever the property is sold.
- The **income approach** focuses more on the potential income that the property can be expected to return in the future. If the same farm in the example above happens to be located right next to a busy interstate connection, than the value of the property is bound to be much higher because the property could potentially be leased to business such as a gas station or restaurant. In this case, the potential future income that the property could generate would be the determining valuation factor.

The appraiser would take all of these factors into consideration, and then prepare a brief report summarizing the findings. The report generally includes a description of the property, a drawing showing the dimensions and square footage of the house (or acreage if land is involved), a brief map showing location, a description of the factors influencing the value of the property, and, an estimate of the property's value.

2. An accurate and formal appraisal is beyond the scope of this lesson, but a discussion of these three main principles is not. Accordingly, tell

your students that they are going to prepare an approximate appraisal of a property of their choosing.

3. Select a property in the community that everyone is familiar with, perhaps even one that is even listed for sale by a realtor (*if all students examine the same property, there may be more competition and incentive to identify the primary factors that determine its value*).
4. Consider having an open discussion concerning the advantages and disadvantages of the property as they affect its value. When the discussion is complete, distribute copies of *Activity Sheet 7-2: Techniques of Real Estate Appraising* to the students. (*Note: Even though they are all evaluating the same property, they may arrive at different conclusions concerning its value.*)
5. When the worksheets are completed, collect the sheets and put the results on the chalkboard in a manner that shows the maximum, minimum, average, and median appraisal values.
6. Invite an appraiser to class to review and comment on the valuations prepared by the students.

Debriefing the Lesson

The purpose of this activity is to familiarize students with some of the techniques and factors considered by a professional real estate appraiser. Students may, or may not, accurately gauge the value, but the value of the exercise is in the process of discovery. The appraiser will probably have thought of some factors that the students missed—and your students may have even considered some factors that the appraiser overlooked.

If possible, ask the appraiser to bring along a sample appraisal for student to examine. Most appraisals follow a standard format, and your guest may be willing to walk the student through the steps he or she would follow to value the property.

LESSON 7-3: PROPERTY APPRAISAL – CHAPTER REVIEW

Consider having your students do a “chapter review” from a real estate appraisal text in their local library. This would be similar to a book review, only it would be confined to a chapter of their selection (*letting them chose the chapter they would review might generate more interest in the assignment*). You may want to assemble a classroom display of materials to pique students' interest and the make the books readily available for student use.

Use a standard book review format, or make one of your own. The report should be a page or two at the most, and would contain the title, author, publication date, and other publishing information. Depending on the situation,

consider using the report as part of a portfolio assignment, or simply treat it as a “good faith” assignment that is primarily reviewed for grammar, spelling, and overall appearance.

Good faith assignments are especially useful in situations where students are likely to examine material that is outside of their (and their teacher’s) area of expertise. The purpose of this assignment is simply to expose them to new material, as mastery of the material at this stage is of less importance than stimulating their interest.

 **Materials Needed:**

- None

 **Teaching the Lesson:**

1. Tell students to find a book on real estate appraising at their local community, college, or university library. Explain that they are to prepare a 1-2 page summary of a chapter of their choice.
2. Review your report format with them, and set a date for them to complete the assignment.

Debriefing the Lesson

Before you collect the assignment, take a few minutes to discuss the chapters selected by the students. Questions concerning the choice of topic, what they liked and did not like, what they would do different in the future are all appropriate. Ask if anyone liked the topic enough to select it as an occupation in the future.

UNIT RESOURCES:

 **Community Resources:**

- Invite a banker or an insurance salesperson to class to talk about how they use real estate appraisals in their business.
- Invite a real estate broker or realtor to class to take about the role of the real estate appraiser in their industry, or:
- Convene a panel consisting of an appraiser, real estate broker, an insurance salesperson, and/or a banker to discuss the importance of real estate appraising to the economy.

 **Teacher Resources:**

- Harrison, Henry S., Standards of Professional Appraisal Practice and Ethics, Harrison's Illustrated Guide, H² Company, New Haven, CT, 1991.
- Ventolo, William L. and Williams, Martha R., Fundamentals of Real Estate Appraisal, Real Estate Education Company, 1990
- Betts, Richard M. and Ely, Silas J., Basic Real Estate Appraisal, Prentice Hall Career and Technology, Englewood Cliffs, 1994.



World Wide Web Resources:

<http://www.appraisalfoundation.org> Site devoted to the improvement of appraisal professionals through the promotion of national qualifications and standards

<http://www.appraisalinstitute.org> Professional institute dedicated to the education, development, and professionalism of real estate appraisers; links to local chapter, publications, research, and frequently asked questions (FAQs)

<http://www.naifa.com> Home page for the National Association of Independent Fee Appraisers; links to appraisals, computers, government, real estate, finance, housing, and search engines

<http://www.EconSources.com/> One of the best portals on the web for general economic information, sources

ACTIVITY SHEET 7-1 THE APPRAISER IN YOUR COMMUNITY

Directions: The best way to find out more about real estate appraisers and the real estate appraisal profession is to ask an expert. For this activity, you are going to visit with a real estate appraiser in your community to find out more about what they do. Several of the questions below are specified for you, but you will need to ask two more of your own. (Note: the two additional questions do not always need to be prepared prior to the interview, they frequently will come up as part of the interview process).



1. What are the educational requirements needed to become a real estate appraiser?

2. Does your state require real estate appraisers to take an examinations or other certification in order to do business?

3. Do appraisers belong to any professional organizations that are designed to improve the quality and reputation of the profession? (*If so, obtain names and descriptions.*)

4. Does the real estate appraisal profession have a “code of ethics” that serves as a guide to its members? (*If so, obtain a short description.*)

5. What do you (the appraiser) like best about your job?

6. Other: _____

7. Other: _____

ACTIVITY SHEET 7-2
TECHNIQUES OF REAL ESTATE APPRAISING

Directions: In this activity, you will try to determine the approximate market value of a property using three popular valuation techniques used by real estate appraisers. Your teacher will provide a brief background on the three techniques; the rest is up to you.



Property to be valued: _____
Location/address: _____

1. The **sales comparison** method: Using the newspaper, internet sites such as <http://realestate.yahoo.com/realestate/homevalues>, or MLS listings of similar properties in your community, try to estimate a reasonable market value.
2. Using the **cost evaluation** approach, try to identify the prior expenditures that should account for some of the property's value.
3. Using the **income evaluation** approach, evaluate the potential income earning aspects of the property (this is more important for commercial property than for residential property).
4. Your estimate of what the property is worth: _____
5. Write a short paragraph explaining how you arrived at your property valuation:
