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Technology spotlight

AVM testing: Seeking a level field

Standardization may be key to meaningful results

As AVM vendors grasp at greater acceptance of their products in the real estate valuation market, the debate is shifting toward testing the technology to ensure lenders and other users are getting an accurate picture in their risk assessment.

This is the first installment in a series looking at the good, the bad and the ugly of AVM testing.

Testing AVMs based on the use and a set valuation matrix will determine which is the best fit. When testing, the sample should include properties that are representative of the types approved for the proposed purpose.

For confidence in AVMs to increase, many industry experts contend there has to be some kind of standardization. To date, efforts to move toward standardization of confidence scores and hit rates have been slow to catch on across the industry. But that may be changing.

Just last year, the Appraisal Institute, the International Association of Assessing Officers (IAAO) and the Collateral Risk Management Consortium (CRC) became the charter members of a new industry task force acting as an informal steering committee to review AVM testing.

The Joint Industry Task Force on Automated
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Business news

Firm launches appraisal franchising

IRR-Residential eyeing chain of independent offices

Following a trail blazed by a number of entrepreneurs, from Ray Kroc to Colonel Sanders, IRR-Residential LLC is girding up to sell residential appraisal franchises nationwide.

Despite the inherent business risks, the Kansas City-based residential appraisal company was recently formed exclusively to develop a national company of independently owned and operated residential appraisal franchises.

The new venture was spawned by Integra Realty Resources Inc. (IRR), an organization for commercial appraisers.

Integra has grown over the past five years to

become the nation's largest commercial real estate valuation and consulting firm, with 54 offices in the United States and Mexico and 740 employees.

Leveraging on the Integra brand, a separate management team developed and launched IRR-Residential to develop and operate a residential real estate appraisal franchise organization, with plans to roll out some 60 franchise offices by the end of the year – just in time for Christmas

“The residential appraisal industry is a very fragmented market dominated by local

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ON DECK

- Does legal flipping have any impact on the valuation process? Only Valuation Review is looking past the surveys to tell you how this trend will impact the industry.
- Is everything peaches and cream in the Lone Star State? Catch our upcoming story on the Texas Appraiser Licensing and Certification Board to find out.

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appraisal firms,” said **Kevin Nunnink**, president of IRR-Residential, LLC and chairman of Integra, based in New York City.

“Their clients have become larger and more distantly located from them. We see an opportunity to develop a company like Integra, where we bring together the best local residential appraisal firms into a national organization that can then re-establish a direct relationship with the clients,” he said.

Nunnink was recently invited to present Integra’s views on the 2005 residential real estate market to Federal Reserve Chairman **Alan Greenspan**, including forecasting potential bubble markets and the impact of those markets on the residential real estate industry.

Not a new idea

“The idea of a national residential company has been in the background thoughts of the organizers of Integra for many years,” said **John Wood**, chief operating officer, IRR-Residential, LLC. “They desired to first build a national commercial appraisal company and then expand into other opportunities that allowed them to further leverage against the success and brand of Integra.”

In researching the residential appraisal opportunity, the company conducted several focus group discussions and also had detailed discussions with individuals who had experience in developing residential brokerage franchise businesses.

“We’ve started discussions with appraisal companies interested in our business concept,” Wood said. “By the end of the year, I think we’ll be in pretty good shape.”

Wood declined to discuss the companies Integra has had conversations with.

Integra has at least one office in every major market in the country. That means

“At the corporate level, we will provide the offices with a brand name identity that will differentiate them in their local markets; regional and national sales and marketing support; and large company buying power.”

— *John Wood, chief operating officer of IRR-Residential LLC*

Integra’s clients can get multiple appraisals or consulting assignments completed anywhere in the country with one phone call, he said.

“IRR-Residential will have similar coverage, but will also cover the secondary markets,” Wood said. “Our goal is to attract the best of the best appraisal offices – those that have demonstrated their expertise in the local market and have a desire to grow their business.”

Wood, however, declined to be more specific as to the company’s modus operandi in accomplishing its goals.

“At the corporate level, we will provide the offices with a brand name identity that will differentiate them in their local markets; regional and national sales and marketing support; and large company buying power,” he said. “Integra has shown that when you bring together many successful local firms into one large national company, everyone benefits from shared business practices.”

However, Wood balked at discussing financing with *Valuation Review*.

“Investments in IRR-Residential are considered confidential, but suffice it to say that it requires substantial investment, and it will be some time before we reach a break even point,” Wood told *Valuation Review*. “However, an attractive element of the franchise business model is that by aligning with successful existing firms, we are able to

grow quickly.”

Franchising — a risky business

Industry experts who asked for confidentiality warn that franchising too soon has led some firms to overextend their resources — and force others into bankruptcy. But Wood isn’t worried.

“Our affiliate offices will already be in the residential appraisal business,” he said. “That’s because we will only hire franchises with appraisers. We are providing them tools including branding, marketing, sales and group buying support to help them expand and grow their business.

“One of the individuals that helped us with our business plan was involved in Coldwell Banker when the company decided to branch out from being a commercial brokerage company, only, into the residential brokerage business,” Wood said. “Like Integra, they developed a strong brand identity and wanted to expand into other endeavors.

“If our affiliate offices are successful, we will be successful,” he added.

AMCs are main competition

Wood was also reluctant to name IRR-Residential’s main competition

“Our primary competitors will be the appraisal management companies,” Wood said. “They have filled a void that was created while lending institutions consolidated, Internet-based lending

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emerged and appraisal ordering was consolidated.

These all combined to place the local-based appraiser at a great distance from an increasing percentage of his clients, he said. The appraisal management companies are the ones with the relationship with large lenders, and in so doing, have taken a significant percentage of the appraiser's fees.

"We see an opportunity to create a large company with national coverage that can then be marketed directly to large lenders as an alternative to the AMCs," Wood said. "Because of the percentage of the residential appraisal business that AMCs control, those businesses are IRR's competition when it comes to soliciting work from large lenders."

Wood was a licensed real estate broker for more than 20 years in Kansas and Missouri and credited with being involved in more than \$150 million of commercial real estate transactions. Prior to joining IRR-Residential in January, Wood was president of First Realty Advisors Inc., a Kansas City-based company that developed software and Internet applications for the commercial appraisal industry.

Matchmaker, make me a match

Integra has the reputation of being a bit of a matchmaker in connecting companies with clients through its regional and national marketing efforts. IRR-Residential hopes to do the same.

"Integra has been very successful with its 'one contact program' for portfolio assignments," said **Jeffrey Rogers**, Integra president and chief operating officer.

"Clients appreciate the ability to facilitate the placement of multiple assignments around the country — with

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Sidebar

Forsythe Appraisals has set industry standard for national expansion plan

If IRR-Residential is looking for a blueprint for success on a national level, they may have to look no further than Minnesota-based Forsythe Appraisals.

Tim Forsythe told *Valuation Review* earlier this year that the company has set its sights on having offices in 40 cities by 2007.

In February, the company opened an office in Houston, the 22nd branch in the United States. And it seemingly proves that Forsythe has developed a business model for success.

Steady growth has been the focus of the company, which opened four new offices — in Spokane and Seattle, Wash., Phoenix, Ariz., and Indianapolis, Ind. — in 2004. It is part of the company's multi-year strategy to increase the number of branch offices it operates across the country.

"The secret to our success has been control. We have consistent service and consistent quality," Forsythe said at that time. "That has been our biggest challenge and our biggest success."

A national presence

Forsythe added that his company has no intent on being a national appraisal company.

Nor should Forsythe's firm be tagged as an appraisal management company. It isn't.

Most recognize Forsythe as one the more successful operators in producing profits with a branch distributive network that employs staff appraisers.

That has been an elusive target for some of the nation's larger companies that have tried to make an appraisal business work

with staff employees.

Most appraisal management firms have historically used appraisal contractors in local markets.

Others have tried

But Forsythe Appraisals may be the exception rather than the rule.

Not so long ago, Primis, a settlement services company out of Atlanta that was subsequently bought by LandAmerica, had a business model which it believed separated the company from competitors.

The model used staff appraisers, inspectors and other specialists as full time employees in brick and mortar offices, compared to most, who offered national settlement services through a managed network of independent contractors.

Given the cyclic nature of real estate, this business model requires a tremendous balancing act between hiring, firing and laying off appraisers during market swings. By the time the dust cleared after a year or two on the acquisition, LandAmerica took a \$30 million write off on its Primis deal due to losses.

Going back further, in the early '90s, TRW's real estate loan services group attempted to build a national network of employed appraisers to deliver appraisal and related valuation services.

The TRW business, burdened by fixed vs. variable labor costs, never turned a profit in the appraisal and valuation business.

By the time TRW divested the business in the mid-1990s, the company was losing 14 percent pretax on annual appraisal revenue of \$75 million. ■

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one contact – knowing that each report will be received on time and contain the local knowledge they need to properly evaluate risk and structure,” he added.

“IRR-Residential is well-capitalized,” Rogers said. “The benefits of our model will be experienced by all of our stockholders. Our franchisees will receive immediate benefits including branding, marketing, cost savings and increased volume.

Earlier this month, Integra announced plans to expand into central New York with the debut of Integra Realty Resources-Syracuse. The new office brings the number of Integra offices to 53 nationwide.

Formerly Kimball Appraisal Group Inc., Integra Realty Resources-Syracuse specializes in industrial, land, office, retail and multi-family appraisals and valuations. The office’s client list currently includes Bank of America, Citibank, HSBC, JP Morgan Chase, Key Bank and M&T Bank.

“We have access to the most up to date information and analysis techniques, locally and globally,” said **William Kimball**, managing director of Integra Realty Resources-Syracuse. “And joining Integra offers us the opportunity to provide a broader range of services to our local and national clients in ways we never imagined.”

Each Integra managing director holds the MAI designation and IRR offers specialty practice in the fields of litigation, hospitality, retail, energy, senior housing and health care and corporate and public finance.

For more information about Integra, appraisers can visit www.irr.com.

Questions? Contact Lori Lesko at llesko@octoberresearch.com ■

Valuation news

In wake of Katrina, Marshall & Swift is educating underinsured Americans

AccuCoverage is an option for appraisers to provide a value for insurance purposes

In the wake of Hurricane Katrina, many Gulf Coast residents are scrambling for their insurance policies.

Many will find that they are underinsured. In the state of Louisiana alone, there are about 1,184,116 homes. According to research by Marshall & Swift/Boeckh, 698,628 of those are estimated to not have enough coverage?.

Linda Jovanelly, director of Marshall & Swift’s Integrated Solutions Group, said MS/B has dealt with the insurance carriers directly, providing them with replacement cost information. Over the last year or so, insurance commissioners from different states contacted Marshall & Swift about the data they provide for insurance carriers and noted that there was no data for the homeowners.

“That prompted us to develop AccuCoverage,” Jovanelly said. “We had been trying to get involved in preparedness projects to let people who live in disaster-prone areas know exactly what replacement costs are.”

MS/B estimates that 59 percent of American homes are undervalued by an average of 22 percent. Jovanelly said that those figures are sobering, considering the devastation that just happened in the Gulf Coast area.

“Some people think it (replacement cost) is based on market value or they may think it is based on what kind of insurance your neighbor has,” she said. “A lot of folks just don’t understand that

two people can have the exact same house and one owner may invest a lot of money redoing the kitchen and the bathroom with the best quality of materials while the other still has standard-grade fixtures. That type of upgrade to a property changes the insurance.”

Having appropriate homeowners insurance is essential. A property owner’s coverage should:

- Completely rebuild the house in the event it is destroyed by a natural disaster
- Replace everything in it
- Protect the owner’s liability in case someone is injured on their property
- Pay for additional living expenses in case of an emergency or disaster that prevents the homeowner from living in your home.

Jovanelly said that an insurance agent should determine replacement cost using a total component methodology instead of square footage methodology.

Total component methodology uses formulas and databases to analyze and select detailed parts of the home to assemble estimates in a risk-specific manner, using localized building codes, structural considerations and local labor and material costs to yield a unique estimate.

It is the homeowner’s responsibility to stay up-to-date on their insurance coverage. There are certain questions homeowners should ask themselves to determine if they need to adjust their

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