Vermont Housing Finance Agency Appraisal Standards

Revised October 2024

Effective January 2025

Background

Vermont Housing Finance Agency (VHFA or Agency) requires appraisals to be completed on all rental housing development projects financed by the Agency. Appraisals are required for projects receiving Low-Income Housing Tax Credits and any type of loan from the Agency.

Appraiser Qualifications and Form of Report

Appraiser Experience and Qualifications

- Be a certified general appraiser under the appraiser certification requirements of Vermont;
- Be in good standing under state certification requirements;
- Be actively and regularly engaged in the appraisal of multifamily properties;
- Have at least three consecutive years of income property appraisal experience;
- Have completed at least one multifamily appraisal in the past 36 months in the geographic market area where the property is located;
- Be knowledgeable concerning current real estate market conditions and financing trends in the geographic market area where the property is located;
- Be experienced in appraising multifamily properties with complexity and characteristics similar to those of the property (such as the number of units and type of property— garden, mid-rise, high-rise, etc.);
- Have a working knowledge of construction costs, materials, methods, and standards in the geographic market area where the property is located;
- Have a strong educational background in appraising income properties. Appraisers must have successfully completed several courses relating to income properties. These courses must have been completed through a nationally recognized appraisal organization or accredited college or university.;
- Be insured.

Applicable Standards

Appraisal must comply with the Uniform Standards of Professional Appraisal Practice (USPAP) as defined by The Appraisal Foundation. In addition to meeting the technical standards of USPAP, appraisers should also ensure they have carefully reviewed USPAP Advisory Opinion AO-14.

"Subsidies and incentives that encourage housing for low- and moderate-income households may create intangible property rights in addition to real property rights and may also create restrictions that modify real property rights. The appraiser should demonstrate the ability to discern the differences between the real and intangible property rights and value the various rights involved. Low-Income Housing Tax Credits (LIHTCs) are an example of an incentive that results in intangible property rights that are not real property but might be included in the appraisal. Project-based rent subsidies are an example of a subsidy accompanied by restrictions that modify real property rights. Appraisers should be aware that tenant-based rent subsidies do not automatically result in a property right to the owner or developer of subsidized housing. Standards Rule 1-2(e) allows the inclusion of intangible assets that are not real property in the appraisal. When personal property, trade fixtures, or intangible items are included in the appraisal, the appraiser must analyze the effect on value of such non-real property items, as required by Standards Rule 1-4(g). A critical factor in all subsidized housing appraisals is the analysis of whether or not the various subsidies, incentives, and restrictions remain with the real

property following a sale or foreclosure and thus are marketable property rights to be included in the appraisal." [1]

Intended Users, Assignments, and Notice of Compliance with Standards

Each appraisal must indicate that (1) the appraiser has reviewed the VHFA's Appraisal Standards, that (2) the appraisal report meets the requirements of VHFA's Appraisal Standards, and (3) the appraiser has the appropriate experience required to competently appraise the subject property.

Vermont Housing Finance Agency (VHFA) is required to be listed as an intended user on an appraisal.

Form and Content of Appraisal

VHFA requires appraisals for rental housing developments to generally comply with report standards outlined in Standards 1 and 2 of USPAP.

Responsibilities of Owners & Developers

Owners and Developers are required to provide appraisers with all requested information needed to complete the appraisal report. At a minimum, owners should proactively prepare the following documents for an appraisal.

1. Property Survey, if available.
2. Rent roll dated within 30 days of the appraisal inspection date, certified by the Borrower as accurate and correct, and containing, at a minimum:
    a. Unit number
    b. Unit type, name, or description and/or unit design (i.e., 2BR/1BA, 1BR/1BA/Den, commercial)
    c. Unit size in square feet
    d. Lease commencement date
    e. Contract rent
    f. Concessions, if any
    g. Additional fees or charges (i.e., pet fees and garage fees)
3. Income and Expense Statements for the previous three calendar or fiscal years, as applicable, certified by the Borrower as complete and accurate
4. Information about existing project reserves, if applicable
5. Year-to-date Income and Expense Statement, certified by the Borrower as complete and accurate
6. Copies of executed commercial leases, amendments and attachments, if applicable
7. Property condition report
8. Environmental report and any information related to proposed environmental remediation (including grants or loans being utilized)
9. Copy of ground leases, if applicable
10. Copy of current sales contracts, if applicable
11. Final architectural plans and specifications if the property is to be built
12. Copies of shared access agreements or easements
13. Regulatory agreements such as HAP contracts or other agreements that might affect the property's rents or expenses
14. Summary of all funding being sought for the project, with special attention to programming that require liens and restrictions
15. Any other information that the Seller/Servicer knows may affect the value of the property

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[1] The Appraisal Institute, Advisory Opinions

Valuation

Required Values

The table below shows the requirements for the timing, required values, and appraisal ordering authority for various combinations of VHFA financing.

Transaction Type	Required Prior to Board Approval	Ordered by VHFA	Required at least 60 days before Construction Closing	Ordered by VHFA
9% LIHTC	As-Is – substantiating land value	No VHFA must be a user	As-Is & As-Complete, both market and restricted (and stabilized)	Yes, if VHFA is a lender or there is no primary lender
4% LIHTC	As-Is – substantiating land value	No VHFA must be a user	As-Is & As Complete, both market and restricted (and stabilized)	Yes, if VHFA is a lender or there is no primary lender
VHFA Loans	As-Is – substantiating land value	No VHFA must be a user	As-Is & As Complete, both market and restricted (and stabilized)	Yes

Regardless of whether VHFA orders an appraisal, the Agency must always be listed as an intended user of the report, and the appraiser must confirm compliance with VHFA Appraisal Standards within the report or in a companion letter.

In no case may the seller or other interested party to the sale other than the credit/loan sponsor order an appraisal.

Land Valuation

If the project is a Low-Income Housing Tax Credit development (LIHTC), the appraisal report must include a land value estimate or allocation for the subject property. VHFA does not necessarily require a land value estimate for other projects. The appraiser is responsible for ascertaining whether the project is being developed under the LIHTC program. The land value should be supported by means of a comparison to similar multifamily development sites. Sales should be identified in the local competitive market area or areas that have similar market conditions relative to the supply and demand, and price levels for this type of development land. Sales should have a similar highest and best use (multifamily development) and should be analyzed by an appropriate unit of comparison, such as price per housing unit. Support should be provided to the degree necessary to enable the reviewer to understand the appraiser's rationale in developing the value estimate.

Valuation Methods and Approaches
Since the appraisal must, at minimum, estimate the as-is leased fee market value of the property, appropriate adjustments are required to any analysis of fee simple data within the appraisal. Examples include:

- Capitalization rates extracted from comparable sales must be consistently applied to the property based on actual or pro forma income. When appropriate, an adjustment must be made to reflect the property's leased fee ownership interests being appraised.

- The traditional Cost Approach is typically developed as a fee simple value; as such, the methodology must be appropriately adjusted to reflect the property's leased fee ownership interest.

- An analysis with 100 percent market rents, without consideration of the property's actual in-place rents, is not a leased fee value estimate.

- Replacement Reserves are required as an operating expense for the purposes of calculation of Net Operating Income (NOI) used in the income approach to value.

- All Low Income Housing Tax Credit appraisals must utilize the Discounted Cash Flow analysis.

- All restricted projects must be valued using market rents for the geographic area in which the property is located, as published by the Office of Housing and Urban Development, adjusted for utility allowance.

- The market approach to value must make two adjustments: (1) for financing, the savings from which are converted to reduce project rents\income, and the present value of this is deducted. (2) for equity distribution restrictions, whereby the difference between a typical equity return is compared to the actual equity return, and the annual difference is converted to a present value estimate, also deducted from the value.

Cost Approach
If developed, the cost approach conclusion must reflect the leased fee ownership interest in the property (or leasehold interest if the property is subject to a ground lease), and the appraiser must include proper adjustments for any items adverse to the property's marketability, such as deferred maintenance, physical deterioration, and functional and economic obsolescence. The Appraiser must specifically describe the estimates of accrued depreciation and entrepreneurial profit. The estimated land value must indicate the market value of the land, recognizing its highest and best use.

If the cost approach is omitted in the appraisal, the appraiser must adequately provide a Property-specific explanation for its omission. Generic statements such as "investors typically do not consider the cost approach when they purchase this type of property" or "there is difficulty estimating depreciation due to current market conditions" are not acceptable and miss the point of the benefits of a cost approach analysis. When appropriate and if not confidential, the appraiser must include sufficient descriptions, including where appropriate, a photograph of the comparable properties to allow the reader of the appraisal to adequately understand the construction similarities between those comparable properties and the property if the appraiser uses cost comparable properties as part of the estimate of replacement cost

Sales Approach
The appraiser must support the value indicated by the sales comparison approach by analyzing the sales of at least four comparable properties. The appraiser may use the property as a comparable sale as long as the appraiser provides four additional comparable properties to the property. The sales comparable properties must be physically and locationally similar to the property and must have been sold recently. The appraiser must make proper adjustments, when necessary, to the sales comparable properties for such items as real property rights conveyed, financing terms, conditions of sale, date of sale, location, physical characteristics, and amenities. The appraiser must adequately explain those adjustments. If there is an absence of recent comparable improved sales, the appraiser must consider that absence when estimating the market value. Current contracts and competitive property listings can be helpful in rounding out the appraiser's analysis if they are indicative of the state of the current market. The weight given to a contract or listing might be different from the weight given to the actual sales transactions, and the appraiser must discuss these differences in the appraisal.

For each comparable used, the appraiser must identify the primary data source(s) used to verify comparable sales data, for example, whether the comparable property's financial and transaction information was gathered as part of the site visit or obtained from an earlier written appraisal by the appraiser's firm, a sales brochure, an individual associated with the sale, or a combination of sources. If the appraiser obtained the comparable property's information from an individual, the appraiser must identify the name, company, and title of the individual, if available. The appraiser may use a multiplier, either a potential gross rent multiplier or an effective gross income multiplier, if the multiplier is customarily used in the property's market area. The appraiser must derive the multiplier from recent sales of comparable properties in the market area of the property. The appraiser must properly analyze the multiplier based on the overall quality and reliability of the gross income the property has produced or is reasonably expected to produce. If the appraiser develops a valuation from a multiplier analysis, it should be reported in the Income Approach (See Income Approach requirements in Section 60.14(c) for additional information.).

The appraiser must not apply an adjustment to the comparable sales for differential net operating income or develop a net income multiplier for the sales since these methodologies duplicate the techniques or value indicators used in direct capitalization in the Income Approach. The Sales Comparison Approach must focus on similarities and differences that affect value, which may include variations in property rights, financing terms, market conditions, and physical characteristics and the causes of income variation, not just that the net operating income of the comparable is different than the property's (either on a per-unit basis or applying a net income multiplier). The appraiser must discuss and adjust for the causes of the differences in NOI, not just note that a difference exists. The appraiser must refrain from adjusting the comparable properties' sale prices for expenses, costs, or renovation that are to be incurred by the buyer after the date of the sale transaction since these costs and expenditures are not typically part of the transaction/consideration price for the property.

Income Approach
The appraiser must derive the value indicated by the income approach by considering the following economic factors:

The forecasted gross income must consider historical rents of the property, current rents of the property, and rents currently obtained from comparable units (similar in amenities, location, size, type, style, and quality) adjusted for market concessions, rent abatements, discounts and the like. The influence and limitations of rent control, rental concessions, historical trends, and other relevant factors must be

reviewed and analyzed relative to the forecasted gross income of the property. The appraiser must analyze and discuss the difference, if any, between the property's actual recent contract rents and the appraiser's estimate of the property's market rents and their impact on the leased fee value of the property. If the appraiser's estimate of market rent is dissimilar to the recent leasing at the property, the appraiser must provide an adequate discussion and explanation of the variance.

The estimated vacancy and collection loss must consider historical data of the property, current data of the property, rental comparable properties in the market area, and anticipated changes in regional market conditions.

The forecasted expenses and Replacement Reserves must be comparable with the historical data of the property and comparable with known and verified expenses in the market area, measured, at a minimum, on a per-unit basis and as a percentage of effective gross income. The identification of the expense of the comparable properties must include, at minimum, the comparable property's number of units, the age of the property (year built and/or renovated), its physical condition, its location, and the time period indicated by the expenses. The forecasted expenses and Replacement Reserves must consider future changes in expense or reserve levels.

The Capitalization Rate must be based on factors reflecting the investment characteristics of typically knowledgeable investors for properties similar to the property.

The appraiser must develop the Capitalization Rate using each of the following techniques, if practicable:

- Extraction from comparable sales with analysis of the comparable properties' variations, if any, from the property's economic and physical characteristics. Capitalization rates extracted by pro forma income or with actual income must be reconciled consistently with the appraiser's estimate of the property's income.

- Published sources (preferably more than one published data source, and preferably a source that focuses on the property's local market, not general national data).

- Personal surveys and interviews with market participants, with the date of the survey and names/titles of the individuals surveyed.

- Band of Investment model (also known as mortgage equity technique) with specific reference to the sources of the financial data assumptions.

- Debt coverage ratio model - with specific reference to the sources of the financial data assumptions.

- The capitalization rate must be supported with comparable sales and with the appraiser's survey/interviews of local real estate participants for knowledge of the property's submarket and investment considerations.

When a multiplier analysis is developed, the appraiser should adequately analyze and discuss the comparability of the comparable sales' multipliers in terms of expense ratios and expenses per unit. Additionally, the comparability of operating expenses should be analyzed and discussed both with and

without the inclusion of real estate taxes since taxes may vary materially between the property's taxing jurisdiction and that of the comparable sale. This variability may have a material effect on the observed multiplier and comparability with the property. The development of a multiplier analysis for the valuation of the property does not exempt the appraiser from adequately analyzing and discussing the property's operating expenses. For Properties with more than 30 units, a multiplier analysis is not recommended; the appraiser should develop a direct capitalization approach. A net operating income multiplier is not acceptable.

A discounted cash flow analysis (DCF) is typically redundant and not required in the development of the income approach for a multifamily property unless the property is not functioning at stabilized operations and/or occupancy.

- If developed, the DCF's cash flow period must reflect the period necessary to achieve stabilized operations unless local practice dictates otherwise. Depending on the time period of unstabilized property operations, it may be developed with monthly, quarterly, or annual cash flows.

- In lieu of, or as a supplement to, a DCF analysis for an unstabilized property, the appraiser can consider the present value of lost revenue, operating expenses, and necessary repairs, renovations, and alterations as adjustments to value.

- Key assumptions used to develop the DCF must be adequately discussed and supported in the appraisal, including rent and expense changes, discount rate, reversion capitalization rate, and absorption period.

In the Income Approach, the value can be developed with either a gross income analysis or direct capitalization analysis; it is not a requirement to include both methodologies in an Appraisal report.

Restrictions and Subsidized Rents

The appraiser must have a firm grasp on each of the impacts of the projected restrictions placed on the property from the proposed funding sources for each valuation. The following information may be helpful in analyzing the restrictions:

1. HAP Contracts Pre-1980: Projects that have the benefit of and which are subject to the original Housing Assistance Program requirements receive rental assistance that was originally based on the financing structure in place at the time of the initial HAP Contract. Projects with the benefit of these older HAP contracts were not restricted to the distributions of surplus cash or access to residual receipts. Cash distributions and access to residual receipts were only restricted by a Regulatory Agreement imposed by VHFA as a condition of its financing. As long as VHFA financing remains in place, distributions and access to residual receipts are restricted. Once the VHFA loan is paid off, all restrictions go away.
2. HAP Contracts Post-1980: HAP Contracts issued after February 1980 were more restrictive than the original HAP Contracts in terms of distributions. The distributions of surplus cash were restricted by the contract. Any remaining surplus cash remains in the project or is returned to HUD at the expiration of the contract. Owners do not have access to cash flows. Their incentive to invest in these properties comes from administrative expenses paid to the owner as well as the anticipated property appreciation, which does not include the value of the residual receipts at the time of sale.
3. Tax Credit Properties: Owners of tax credit properties are always Limited Partnerships. Distributions of surplus cash are defined and restricted under the terms of a Regulatory Agreement. Any project ending its initial 15-year term may be sold for "market value"; however,

rent levels and cash distributions will continue to be restricted through the extended use period. Most Tax Credit transactions now require "perpetual affordability", meaning the project will remain in the affordable housing stock for its entire useful life. The appraiser should take special care to denote if perpetual affordability is required for the subject property.

Subsidized rents should not consider hypothetical conditions and extraordinary assumptions. However, VHFA will allow the As-Is Value to be based on increased rents (effective by closing) in a HAP contract as long as the applicant includes the following: (1) a copy of the submission to HUD requesting the rent increase, (2) comfort letter or approval from HUD.

Market Information

The appraiser must include market information sufficient to substantiate the building's value and occupancy rate. When the appraiser selects comparable projects to analyze absorption rates, similarly restricted properties should be identified in the market area.

Environmental Remediation

Federally funded projects may require a deeper level of environmental review and remediation activities than a market transaction. When environmental remediation costs are identified as part of the development plan for a parcel, the Appraiser should closely review the terms of any state or federal funding used to remediate the environmental concerns. Appraisers should review USPAP Advisory Opinion 9 (AO-9) "Appraisal of Real Property That May Be Impacted By Environmental Contamination" and the Appraisal Institute's Guide Note 6 (GN-6) "Consideration of Hazardous Substances in the Appraisal Process." The known value and availability of state/federal resources committed to the remediation process must be documented. To the extent possible, similar sales of properties requiring remediation should be used to establish a market value.

Expense Analysis

Expense Analysis must include a review of actual expenses for the subject (if applicable), along with the owner's projected budget, which must be reported, summarized, and analyzed. A copy of the actual operating statements analyzed must be included in the appendix. If such data is unavailable, a statement to this effect is required, and appropriate assumptions and limiting conditions must be made. Expenses of three similar comparable properties with similar restrictive rent structures and services plans are required. The identity of the expense comparable properties may be identified as confidential but must be available if requested and appropriate. Historical expenses of published survey data for similar properties may be used at the discretion of the appraiser. Any expense differences must be reconciled.

The following expenses must be considered: Management Salaries (full-time or part-time); maintenance Salaries (full-time or part-time); other Employees Salaries (full-time or part-time); employee benefits; office supplies; telephone; travel; leased furniture; support services; legal; accounting; advertising; contract repairs; general repairs; grounds maintenance; extermination; maintenance supplies; elevator maintenance; redecorating; water expenses paid by landlord; sewer expenses paid by landlord; electricity expenses paid by landlord; gas expenses paid by landlord; common area utilities (water, sewer, electricity, gas); trash collection; real estate taxes (consider tax freeze if applicable); insurance premiums; special assessments; security staff or security system; management fee; reserves.

Three tax-comparable projects are required in which the land and improvements are separated, and the analysis used to derive estimated taxes for the subject must be included. A tax plat of the property shall be included as an appendix in the report.

Glossary of Terms

Area Median Income (AMI): Median family income for a particular county or metropolitan statistical area (MSA), as estimated by HUD. HUD, each year for each area, also publishes a revised estimate of the income limit for a very low-income (VLI) household, defined as 50 percent of the estimated AMI. LIHTC tenant income and rent limits are based on this VLI amount, which may or may not exactly equal 50 percent of the estimated AMI for the area

Basic Rent: The minimum monthly rent that tenants who do not have rental assistance pay to lease units developed through the USDA-RD Section 515 Program, the HUD Section 236 Program, and the HUD Section 223(d)(3) Below Market Interest Rate Program. The basic rent is calculated as the amount of rent required to operate the property, maintain debt service on a subsidized mortgage with a below-market interest rate, and provide a return on equity to the developer in accordance with the regulatory documents governing the property.

Capitalization Rate: Any rate used to convert income into value.

Capture Rate: The percentage of age, size, and income-qualified renter households in the primary market area that the property must capture to fill the units. Funding agencies may require restrictions to the qualified households used in the calculation, including age, income, living in substandard housing, and other comparable factors. The capture rate is calculated by dividing the total number of units at the property by the total number of age, size, and income-qualified renter households in the primary market area. See also: penetration rate.

Change Rate (CR): The rate of stabilized change in property value and/or income.

Comparable Property: A property that is representative of the rental housing choices of the subject's primary market area and that is similar in construction, size, amenities, location, and/or age. Comparable and competitive properties are generally used to derive market rent and to evaluate the subject's position in the market. See the National Council of Affordable Housing Market Analysts' white paper "Selecting Comparable Properties."

Competitive Property: A property that is comparable to the subject and that competes at nearly the same rent levels and tenant profile, such as age, family, or income.

Contract Rent: (1) The actual monthly rent payable by the tenant, including any rent subsidy paid on behalf of the tenant to the owner, inclusive of all terms of the lease. (HUD & RD). (2) The monthly rent agreed to between a tenant and a landlord.

Demand: The total number of households in a defined market area that would potentially move into the proposed new or renovated housing units. These households must be of the appropriate age, income, tenure, and size for a specific proposed development. Components of demand vary and can include household growth, turnover, those living in substandard conditions, rent over- burdened households, and demolished housing units. Demand is project specific.

Direct capitalization: (1) A method used to convert an estimate of a single year's income expectancy into an indication of value in one direct step, either by dividing the income estimate by an appropriate rate or by multiplying the income estimate by an appropriate factor. (2) A capitalization technique that

employs capitalization rates and multipliers extracted from sales. Only the first year's income is considered. Yield and value change are implied but not identified.

Elderly, Senior, or Age-Specific Housing: Housing where (1) all the units in the property are restricted for occupancy by persons 62 years of age or older or (2) at least 80 percent of the units in each building are restricted for occupancy by households where at least one household member is 55 years of age or older and the housing is designed with amenities and facilities designed to meet the needs of senior citizens.

Extremely Low Income: A person or household with income below 30 percent of AMI adjusted for household size.

Fair Market Rent (FMR): The estimates established by HUD of the gross rents (contact rent plus tenant-paid utilities) needed to obtain modest rental units in an acceptable condition in a specific county or metropolitan statistical area. HUD generally sets FMR so that 40 percent of the rental units have rents below the FMR. In rental markets with a shortage of lower priced rental units, HUD may approve the use of FMRs that are as high as the 50th percentile of rents.

Gross Rent: The monthly housing cost to a tenant, which equals the contract rent provided for in the lease plus the estimated cost of all tenant-paid utilities.

Housing Choice Voucher (Section 8 Program): Federal rent subsidy program under Section 8 of the U.S. Housing Act, which issues rent vouchers to eligible households to use in the housing of their choice. The voucher payment subsidizes the difference between the gross rent and the tenant's contribution of 30 percent of adjusted income or 10 percent of gross income, whichever is greater. In cases where 30 percent of the tenant's income is less than the utility allowance, the tenant will receive an assistance payment. In other cases, the tenant is responsible for paying his share of the rent each month.

HUD Section 202 Program: Federal program that provides direct capital assistance (i.e., grant) and operating or rental assistance to finance housing designed for occupancy by elderly households who have income not exceeding 50 percent of AMI. The program is limited to housing owned by 501(c)(3) nonprofit organizations or by limited partnerships where the sole general partner is a 501(c)(3) nonprofit organization. Units receive HUD project-based rental assistance that enables tenants to occupy units at rents based on 30 percent of tenant income.

HUD Section 236 Program: A federal program that provides interest reduction payments for loans that finance housing targeted to households with income not exceeding 80 percent of AMI who pay rent equal to the greater of basic rent or 30 percent of their adjusted income. All rents are capped at a HUD-approved market rent.

HUD Section 8 Program: Federal program that provides project-based rental assistance. Under this program, HUD contracts directly with the owner for the payment of the difference between the contract rent and a specified percentage of the tenant's adjusted income.

Utility Allowance: The amount that is credited against the maximum allowable rent for resident-paid utilities. Utility allowances are provided by Local Housing Authorities and or the State Housing Authority.

Yield And Change Formula: Method of deriving a capitalization rate by deducting the rate of stabilized change in property value and/or income from the yield rate (R = Y - CR)

Yield Capitalization: The capitalization method used to convert future benefits into present value by discounting each future benefit at an appropriate yield rate or by developing an overall rate that explicitly reflects the investment's income pattern, value change, and yield rate.

Yield Rate (Y): A rate of return on capital, usually expressed as a compound annual percentage rate. A yield rate considers all expected property benefits, including the proceeds from the sale at the termination of the investment.