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## APPRAISING

### Understanding the Appraisal Process: Sales Comparison and Paired-sales Analysis

MOBILITY Magazine, September 2001

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*Martin explains the fine art of doing the sales comparison and paired-sales analysis that is performed when appraising a home. He takes a look at best practices to use when using comparables in regard to market condition, date of contract, and home improvement costs.*

For transferees, the relocation appraisal process and use of the ERC Residential Appraisal Report form might sound like a bunch of technical wizardry. The basic aspects of the sales comparison analysis and the use of paired sales are the heart and soul of the appraisal process, particularly for single-family homes.

In determining what adjustments are made within the sales comparison analysis, finding paired sales is the basis for which adjustments are made.

In preparing for the sales comparison analysis, the appraiser first derives the physical, functional, and location characteristics of the subject based on a personal inspection of the interior and exterior of the subject property and details provided by the transferee.

Also, before preparing the subject data for the sales grid portion of the ERC Residential Appraisal Report form, information about the economics of the subject marketing area, zoning, flood hazard information, and other general neighborhood data are analyzed.

The data entered into the sales comparison grid give the appraiser the basics needed to begin the research for comparable sales within the subject marketing area. All available sales data sources available to the appraiser within the regular course of business are evaluated. The appraiser reviews available listings including active, expired, cancelled, pending, withdrawn, and sold properties.

Available sources for sales data may be researched and verified through a combination of the following: local Multiple Listing Services, assessors' offices, independent data verification services, local builders and contractors, developers, title companies, buyers, sellers, Realtors, appraisers, and past appraisals performed by the appraiser.

After review of available comparable sales data of arm's-length transactions within the subject market, the appraiser chooses sales that are most comparable to the subject property. Then, the sales are put in a grid type format with the ERC appraisal report form. The data that is believed to be most relevant for comparative purposes is analyzed in the same format as the subject that has been input within the sales comparison grid.

After each sale has been entered into the sales grid of the ERC Residential Appraisal Report form for comparison, the appraiser is able to readily identify differences between the subject property and comparables chosen for analysis, those most similar and competitive to the subject property.

Ideally, the appraiser uses the principle of substitution, identifying properties that have sold within the market that are reasonable substitutes for the subject property. As market-derived, relevant characteristics within the sales grid for each of the comparable properties are compared to the subject property, each of the differences found with the comparables are considered and adjusted where appropriate to mirror the subject.

Only those differences that are recognized by the majority of buyers willing to pay more or less for the improvement are adjusted upward or downward in terms of price within the market of the subject property. These items are then adjusted for within the sales comparison grid.

Adjustments for financing or seller concessions are made first. That way, each of the sales transactions is equalized in terms of cash. In that manner, prior to all other adjustments made, the comparables are first equalized to the method of financing that is

typical for the market in which it is located.

The financing adjustment, if any, is then followed by the date of contract. The date of contract is important to remember, because some appraisers have mistakenly used the settlement date when the property closes.

In some situations, the difference between the contract and settlement date may be minimal or non-existent, especially in a rapidly moving market.

Additionally in some transactions, particularly those involving new construction, the settlement date may follow months later. After adjustments are made for the financing/ conditions of sale and date of contract, the adjustments are made for all other pertinent market-recognized differences.

In some instances, there may be differences where the market may not pay for an improvement and may even cause a diminution in value.

This happens, despite substantial cost for improvements such as heavily personalized decorating in most markets; pools in many northern United States; and general over-improvements that exceed what most buyers would prefer in a particular market area.

In determining adjustments for the sales analysis within the ERC Residential Appraisal Report form, the appraiser researches the market for paired or matched sales within the market. These sales must be as nearly identical as possible so that the appraisal can readily isolate small differences and determine from nearly identical properties what the market is willing to pay for a difference between the subject property and a comparable used within the sales analysis.

For example, in a large tract development, there may have been multiple recent sales of the same model for which the only basic difference may be sales with two-car garages and sales with three-car garages.

By pairing several matched sales, the appraiser is able to observe differences paid in multiple transactions for the difference of the number of garage spaces.

Thus, given the following information: Sale A sells for \$297,000 with a two-car garage; Sale B sells for \$297,500 with a two-car garage; Sale C sells for \$302,500 with a three-car garage; and sale D sells for \$303,000 with a three-car garage. The sales data, assuming no other differences, and all being current sales would indicate the following:

Matching A with C and D indicates a premium of \$5,500 and \$6,000, respectively, and matching B with C and D indicates a premium of \$5,000 and \$5,500, respectively.

Analyzing the data, the mean, median, and mode all indicate a premium of \$5,500 is paid for having a three-car garage as compared to having a two-car garage.

Although it is nearly impossible to perform an objective paired-sales analysis on every comparable for every difference to the subject property, this is the basis for which adjustments are to be derived within the market. In highly unique properties, in which there are significant differences between the subject and comparable properties, a matched-pair or paired-sales analysis to determine adjustments for the sales comparison grid may be nearly impossible.

Appraisers instead use expertise garnered from completing years of appraisals as the source for making market-based estimates for the adjustment to each of the comparable sales within the sales comparison analysis.

Ultimately, as the sales grid is completed, each sale is reconciled in comparison to the subject property to formulate a range in value and ultimately an indication of the "anticipated sales price" for the subject property. The sale or sales most nearly identical to the subject may be given primary emphasis as the value is reconciled, with some consideration given to each of the sales that are relevant.

Also considered are active or pending listings that indicate the available supply of homes, potential list price for the subject, and direction of the market.

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