Nationwide
Appraisal
Network

Simple. Smart. Solid.

The TOP 10 questions Borrowers ask Lenders & Appraisal Management Companies

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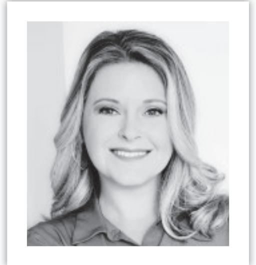
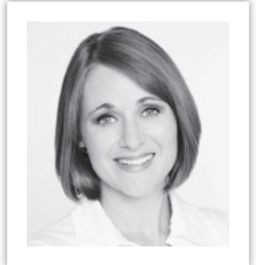
ABOUT THE AUTHORS



Joni Pilgrim

Joni Pilgrim is one of the founding partners of Nationwide Appraisal Network. She has served many roles in the company since the doors opened, including Director of Operations. In 2011, she decided to take on the role of managing sales and marketing. "Our brand is dynamic, young, and smart. We want people to be excited to work with NAN. We are a company built upon the people that work here. I want to let the industry know that this is what makes us different." Business development and brand awareness is the main focus of her daily life at NAN.



Cristy Conolly

Cristy Conolly is the Director of Quality Assurance & Compliance at NAN. As the head of NAN's Compliance Department, she makes sure the standards stay high and ensures NAN's integrity. As a Certified Residential Appraiser, Cristy understands the challenges faced by the ground level appraisers up through the clients' board rooms. "NAN creates a relationship with its clients and appraisers where compliance and exceeding quality standards work together seamlessly, while never sacrificing integrity or our commitment." Making compliance easier on everyone and understood by all is one of Cristy's core competencies that she brings to NAN on a daily basis.

Kevin Johnson

Kevin directs our sales efforts at Nationwide Appraisal Network. Kevin came to us from the West Coast with more than 24 years of experience in the mortgage industry, including a diverse background in wholesale and correspondent lending, as well as, underwriting and operations. Kevin's role at NAN is vital in developing sales and client relations. He leads the on boarding process as well as on-going training and support for our new and existing lender clients.

INTRODUCTION

How to understand Appraisals

The complex subject of property appraisals can be daunting for borrowers. As an Appraisal Management Company we get many questions about how Appraisals work and what the process involves.

This document provides an easy-to-follow guide to the unfamiliar terminology and information most people seldom have cause to deal with.

Regulation Requirements

Now more than ever, the appraisal industry is a highly regulated business thanks in part to the financial crash of 2007, and most of the complicated procedures that have to be followed are due to the Regulations.

This past January (Effective January 18, 2014), a new regulation regarding disclosure and delivery requirements for copies of appraisals and other written valuations under the CFPB and the Equal Credit Opportunity Act (Regulation B) was issued. The requirement states that creditors must provide applicants a copy of ALL appraisals and other written valuations developed in connection with an application for credit to be secured by a first lien on a dwelling.

This means that you, as a borrower, may have questions regarding the information and conclusions in your property's Appraisal. When you receive the appraisal report, you may find it very confusing. We hope that our little book will help you understand more about how it works.

What is an Appraisal?

An appraisal is simply "an opinion of value". The appraised value and some information contained in the report are the opinions of the appraiser signing the report. In fact if two appraisers complete an appraisal on the same property on the same day, the values aren't likely to be exactly the same. Typically when an appraisal is completed for a refinance or line of equity, the value needed is a current market value.

The appraiser has requirements from different entities they must meet, for example: specific instructions provided by the lender. (Fannie Mae, Freddie Mac, VA, and FHA all have their own specific requirements) . There is also USPAP, the authority on appraising, for the appraiser to comply with.

The appraisal is a reflection of current market conditions, so it is important to understand that you cannot compare your property to a house similar to yours that sold in the past.

On the next pages you'll see the top ten questions we are asked by Borrowers, and we hope our answers will help you to understand more about appraisal reports!

#10 QUESTION:

How is the value of my property determined?

You'll be surprised to learn that more of the appraisers work is completed through research than in the field!

The appraiser will research the market area to determine if property values are increasing, decreasing, or remaining stable. They need to know neighborhood trends and what the current inventory of available housing is. They research public records to obtain information on the property and to ensure it complies with local zoning, among other things.

During the visit to the property when the appraiser completes their inspection, they will physically measure the property. This is where the GLA is obtained – NOT from public records or the tax assessor. The appraiser must measure the property themselves and report their measurements in an interior appraisal. During the inspection, the appraiser will note materials in each room, condition of everything, any amenities, or external items that impact value (i.e., railroad tracks behind the house, a gas station across the street).

Once the appraiser has inspected the property, they will search for comparable properties through the MLS and other local data sources. The properties sought will be as similar as possible in regards to design, GLA, room count, condition and amenities. They may also talk to local real estate professionals active in the market. Once the overall most similar comparables have been selected, the appraiser must drive by each of them to observe any external influences that will impact value.

Two properties are rarely exact matches and the appraiser is typically limited to what has sold within the last year, so the appraiser must adjust for any differences that the market shows to impact value. Adjustments come up a lot in conversations as well and we will talk about how they are made later on.

Once all of their research is concluded, the appraiser will complete the appraisal report and develop their opinion of value.

#9 QUESTION:

The Cost approach. What is it?

This is another method an appraiser may use to develop an opinion of value.

In a nutshell, it's a breakdown of what the cost would be to rebuild the property today if it were destroyed. The appraiser has two options to select from – **Reproduction Cost** or **Replacement Cost New. Reproduction Cost** is used if an exact replica of the original property is produced. **Replacement Cost New** is used if a property is rebuilt with comparable utility, but using current design and construction methods and materials. You will almost always see appraisers select **Replacement Cost New.** But it's not that cut and dried, the appraiser also takes in to account the land value and any deduction or additional value for depreciation or appreciation.

The cost approach is a valuable method to use when appraising newer homes that might have little or no depreciation; however for homes older than a few years, it is not generally considered very reliable. Some underwriters still want these completed regardless of the age of the home, and that's when we start running into confusion from borrowers. **There is a big difference between the cost of building a home today versus 30 or 40 years ago.**

Let's break it down:

First, we have the site value. This is the value of the land minus any improvements and is typically determined by vacant land sales in the market area.

Next, there is the cost to construct the dwelling which may confuse borrowers who often assume that this cost per square foot should equal what their home's value is per square foot. This is not the case – it is actually showing what it would cost per square foot to build this home today as new construction, using today's materials. The age of the home has not yet been taken into account.

Following the construction cost of the dwelling, the appraiser will add value for any additional improvements such as an in-ground pool, or a porch at what their cost new would be at today's prices.

Next, the appraiser has to consider depreciation-which takes into account the age and condition of the property, as well as any functional or external obsolescence (for example, railroad tracks, commercial influence, only having access to the bath through a bedroom).

Finally, in order to arrive at an estimated value of the property the appraiser has to consider the "as is" value of site improvements, which could include driveways, private wells, sewer systems, etc.

Together all of these items described provide the appraiser with an estimated value of the cost to reconstruct the same property.

FHA	Conventional	
✓	✗	A Case number
✓	✗	Attic and Crawl Space inspections
✓	✗	Peeling paint inspection for properties built prior to 1978
✓	✓	Uad format
✓	✗	A panel of dedicated certified appraisers
✓	✗	A long detailed list of MPS
✓	✓	All health or safety hazards to be corrected

#8 QUESTION:

What's the difference between an FHA appraisal and a conventional appraisal?

FHA and conventional appraisals used to have vastly different guidelines and requirements. Over the last few years, the industry as a whole has tightened appraisal guidelines, while FHA loosened theirs in 2005. These changes have blurred the once distinct line between FHA and conventional appraisal specifications.

One major difference is FHA maintains its own panel of approved appraisers. If an appraiser is not FHA certified, they are not permitted to complete an FHA appraisal.

In addition, FHA requires the appraiser to do a more thorough inspection of the property. On a conventional appraisal, the appraiser is only required to complete the report "subject to" items that affect the safety, soundness, or structural integrity of the property.

Above and beyond these items, FHA has Minimum Property Standards that must be met in order for them to insure the loan. Though FHA emphasizes that an appraisal is not a home inspection, they do require additional reporting to verify the condition of the home. Due to this, an FHA appraiser must complete the appraisal "subject to" completion of any required repairs or inspections based on FHA MPS (minimum property standards). An appraisal completed "subject to" means there are items that must be completed prior to your loan closing. A final inspection will be necessary, which is an additional cost.

Let's take a look at some items required in FHA appraisals vs. conventional appraisals:

All FHA appraisals will have a Case number, which is how HUD (housing and urban development) tracks the property for the life of the loan.

Attic and Crawl Space inspections are required for FHA but not conventional. FHA requires the appraiser to do at least a head and shoulders inspection of any attic or crawl spaces to observe and report any deficiencies. This is something you should know ahead of time if you're applying for an FHA loan. You will need to provide access for the appraiser to view the attic and crawl space during the inspection – even if the attic is a scuttle located in a closet.

Peeling paint is another FHA requirement for any property built prior to 1978. If any paint on the interior or exterior is chipped or peeling, it must be repaired due to the possibility of lead.

Both FHA and conventional appraisals are required to be in UAD (uniform appraisal dataset) format, which will be explained in Question #6.

To summarize:

FHA has its own panel of certified appraisers that must complete their appraisals, while Fannie Mae does not. FHA also has a longer, more detailed list of minimum property standards than conventional. And finally, both FHA and conventional require any health or safety hazards to be corrected prior to funding the loan.

#7 QUESTION:

My property is Rural and/or Unique, how will my appraisal be affected?

Appraisers face particular challenges when appraising properties located in small towns and rural areas or structures that are unique in design. So much so that Fannie Mae recently released a Lender Letter addressing these challenges.

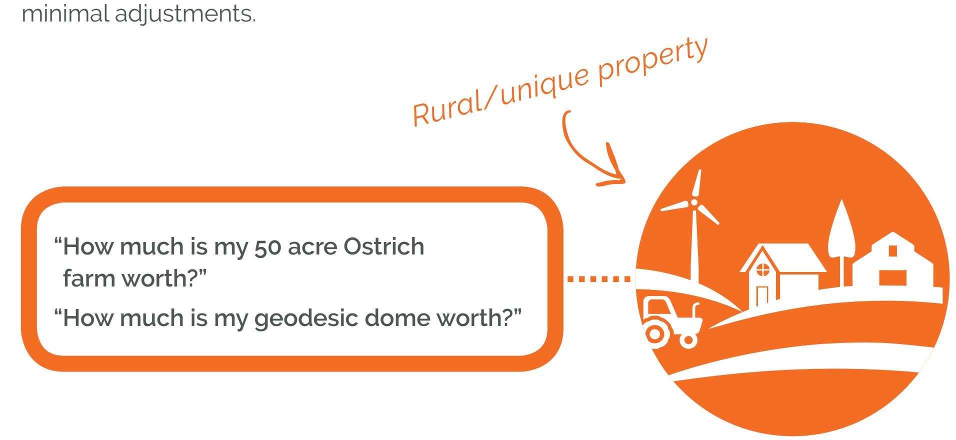

FannieMae

Lender Letter LL-2014-02

March 25, 2014

To: All Fannie Mae Single-Family Sellers

The availability of suitable sales for comparison can be challenging due to limited market activity and possible scarcity of sales. An appraiser can only use what is available to them, which sometimes means the comparable properties will be dated, distant, and have adjustments that exceed industry guidelines. It's common to see comparable properties as far as 20 miles away, greater than one year old and with over 50% gross adjustments. Rural areas or unique designs are also challenging for the underwriter, since they don't fit into the idealistic appraisal box where every comparable property is within 1 mile, sold in the last 6 months and has minimal adjustments.



In these cases, it's important for the appraiser to locate comparable properties that demonstrate the as many of the same dominant features as the property being appraised. For example, if the property is on 25 acres, the comparable properties need to be on similar acreage to support value and demonstrate marketability. If the property is a geodesic dome, it needs to be compared to properties of similar design. The underwriter needs to see that the property value is supported by the comparables used.

#6 QUESTION:

Why are adjustments made when comparing similar sales to my home?

In developing an opinion of value, the appraiser considers recent sales of similar properties called Comparables. Rarely are two properties exactly the same, therefore the appraiser must account for differences between the properties that sold and the property being appraised. These differences are called "adjustments." Adjustments are added or subtracted from the sales prices of the comparable to indicate adjusted sales prices. The adjusted sales prices of the comparables will reflect the probable range of value for the subject.

Some adjustments you'll see are GLA (gross living area) differences greater than 100 SF (square foot), 1 car garage vs. 2 car garage, varying bathroom counts, quality or condition.

It's important to note the cost to complete an upgrade or improvement does not always equal added value to the home.

The adjustments are derived from market data that supports what the typical buyer is willing to pay for these differences. A great example of this is an in-ground pool. A typical buyer will rarely pay what it cost to put in, especially in the northern part of the country where they can't be utilized most of the year.

Two very confusing adjustments since implementation of the UAD are those for quality and condition. The UAD requires the appraiser to utilize 1 of 6 options for these two items. Properties must be reported with the most accurate overall rating. This means that the property being appraised and a comparable may both be in overall C3 condition, however the comparable might have some inferior or superior upgrades.

Although the overall condition rating is the same, there will be an adjustment to account for the differences in upgrades.

In these cases, the appraiser needs to include comments clearly explaining this in the report. Ideally all features and amenities the subject has will be bracketed by the comparables selected. While this is not an appraisal requirement – USPAP, FHA, Fannie and Freddie do NOT require bracketing – it is typically an underwriting requirement for the lender. If bracketing is not possible, the appraiser should explain why in the report.

#5 QUESTION:

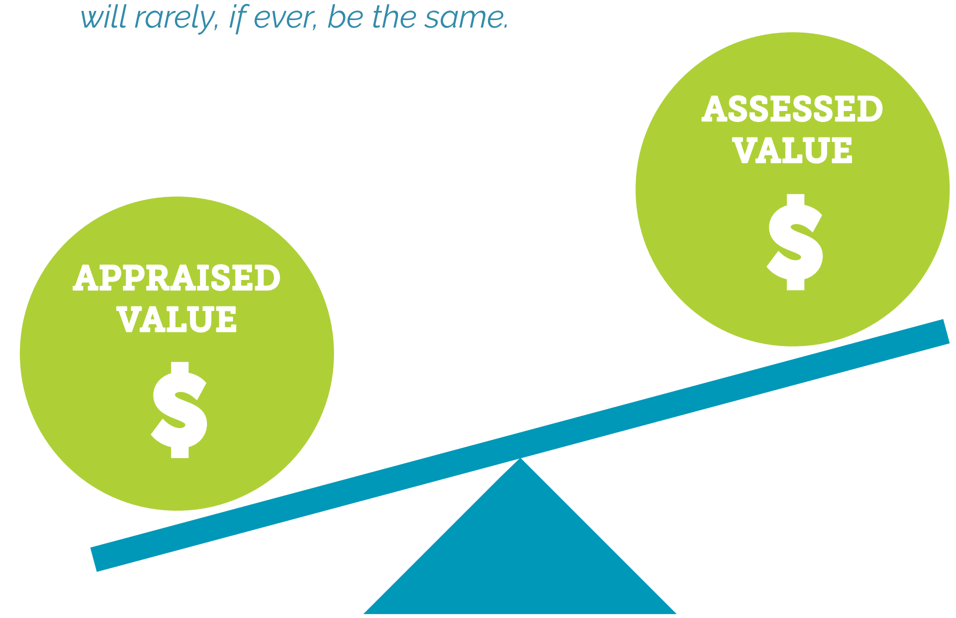
Why are my assessed value and my appraised value different?

An assessment is the value placed on a property by the assessor's office as a basis to determine the property tax due. The assessor typically does not complete an appraisal to determine this, nor are they bound by the same requirements that appraisers are. They usually do not do an interior inspection to take into account the condition of the property or to confirm measurements the 2nd or 3rd stories.

For example, if there is a 2 story foyer or family room, they would not know this and would inadvertently inflate the GLA. Assessments may often be outdated as well, since they are not typically done on a yearly basis.

An appraisal, on the other hand, is completed by a state licensed or certified appraiser and is reflective of the current market value of the property. The appraiser takes into account every detail of the entire property, inside and out, along with current market conditions and sales to determine a value.
The assessed value is not a factor that is considered by an appraiser.

Assessed value and appraised value will rarely, if ever, be the same.



#4 QUESTION:

How are my upgrades and improvements valued in my appraisal?

Buyers, sellers and anyone seeking to refinance a house or take out an equity line of credit might assume that certain home improvements affect appraisal values, but the results will often surprise them.

Cosmetic upgrades to a home can impact the value, depending on what they are. Replacing hard wood flooring with tile will likely not impact the value, as this is a personal preference. On the other hand, if you replace worn out 20 year old carpets with top of the line hard wood, that will likely impact the overall condition of the property, which is considered in the value.

Most times, cosmetic upgrades are a matter of personal preference and not necessarily recognized by the market. For this reason, Homeowners sometimes create an over-improvement where the expense of improving the property is excessive in comparison to other properties in the market and won't be financially recouped. As an example in one case, a borrower put in a 24 karat gold faucet in the bathroomand wanted to know why there was no added value given in the appraisal. The answer? This is not typically something a typical buyer would be willing to pay extra for when purchasing a home.

Examples of home improvements that will have a major impact on the appraisal would be additions including baths and bedrooms, major structural upgrades such as replacement of a worn roof, or stabilization of a crumbling foundation. The market expects these items to be upgraded over time to keep the property in average or better condition. Without replacing or updating items when they're in disrepair, the home's value will suffer. Conversely, some improvements, like removing a bedroom to expand a closet, or combining two smaller bathrooms into one large one, may actually hurt the value.

A good example would be when a borrower spends $40,000 remodeling their kitchen and yet the appraisal doesn't give credit for the amount invested. This is a classic case where the cost of the upgrade does not translate into value. While a brand new kitchen will have an impact on the value, it will not be dollar for dollar. In this case, the property would be compared to other properties that also had remodeled kitchens of similar quality to reflect what the market value of this improvement is.

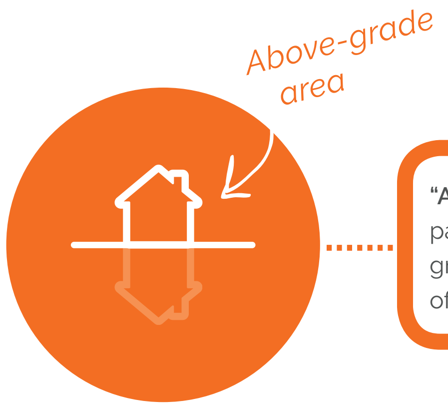
Another important factor many borrowers don't realize is that any improvements that are not permanent are considered personal property and therefore not usually valued in the appraisal. Examples would be an above ground pool, a shed that is not on a permanent foundation or a hot tub. These items would not necessarily be included or valued in the appraisal.

#3 QUESTION:

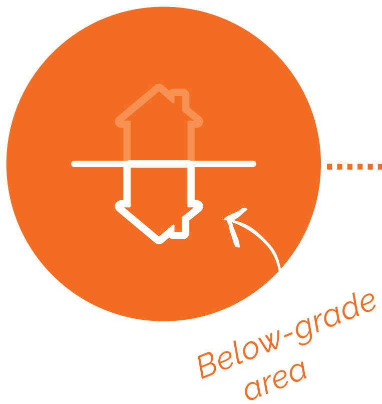
What is the difference between valuing above grade vs. below grade square footage?

One of the questions we are most often asked is why a basement or level partially below grade was not counted in the GLA and overall room count.

Let's start with defining the 2 areas:



"Above grade area" refers to that finished part of the dwelling that is above the ground line, or grade of the earth. Think of the first floor and any floors above.



"Below grade area" is usually defined as the area that is all or partly below that ground line. Think basement space. Even if that space has windows it is considered below-grade.

Above-grade and Below-grade are defined as distinct areas and the appraiser will report and value them separately on the sales comparison grid. Only finished above-grade areas should be used in calculating and reporting above-grade room count and GLA. Fannie Mae considers a level to be below-grade if **any** portion of it is below-grade, **regardless** of the quality of its finish or the window area of any room. Therefore, a **walk-out basement** with finished rooms would not be included in the above-grade room count. This would be given value as a finished basement.

#2 QUESTION:

I'm going with a new lender; can you change the name of the lender on my appraisal to reflect this?

One of the things we hear a lot from borrowers and sometimes lenders is – The borrower switched lenders, and we need the appraiser to change the lender name. Can the appraiser just switch it without having to do a new assignment?

The answer is no – this is a USPAP. USPAP requires a new assignment if the lender/client changes. If the appraiser simply switches the lender name, they are in violation of USPAP and putting their appraisal license at risk. In order to comply with USPAP, there must be a new assignment ordered by the new lender/client.

Borrowers sometimes ask: I'm the one that paid for this appraisal – can't you just give me a copy of it?" But again, this is a USPAP issue. USPAP mandates that the appraiser must not disclose confidential information or assignment results to anyone other than the client or those specifically authorized by the client. Without consent from the lender, neither the appraiser nor the AMC can provide the report to the borrower or discuss it with them.

#1 QUESTION:

What do I do if I find errors or have concerns?

First, you should contact your lender describing the error found and any factual support you have. Errors could be incorrect bed/bath count, a large discrepancy on square footage reported, etc.

If you believe the appraiser selected comparables that were not the most similar, submit a list of closed sales to be considered. Be aware however: active listings do not support a different value. Until they are sold, the market has not accepted that price. Nobody knows if it will sell at all, or if it does, at what price.

All of the information the borrower provides will be relayed to the appraiser who will then review and respond. If after disputing an appraisal, the borrower still feels it is not accurate, there are a few options.

1

First, you could order an appraisal review-this is when another local appraiser reviews the report to verify data and provides their opinion on the comps selected and the value. If they feel there were better comps or the value is not supported, they will note this in the review. Depending on the type of review ordered, the review appraiser may also provide additional comps and their own opinion of value.

2

You could also order a full 2nd appraisal, which is completely separate from the original appraisal. This would give you a new report from another local appraiser to determine their opinion of value. Generally speaking, if appraisals are completed around the same time, the values should be within 10% of each other. Remember, appraisals are opinions, so the values will not match exactly

An important thing to remember when ordering a 2nd appraisal is AIR (Appraiser Independence Requirement). AIR does not allow a 2nd appraisal to be ordered unless one of the following criteria has been met:

1. The 1st appraisal is flawed and the reasons why are clearly documented in the file
2. It's part of the lender's pre-established appraisal review or QC process
3. A 2nd appraisal is required by law

Make sure you have these bases covered if you choose to order a 2nd appraisal.

GLOSSARY:

Adjusted Sales Price: Reflects what the sale price of a Comparable would be after adjusting for the different characteristics between the Comparable property and the Subject property. Since no two properties are identical, the appraiser analyzes a large number of sales to find data to reflect the market reaction.

Adjustments: A calculation that reflects the market's reaction to the difference in properties.

Appraisal: The act or process of developing an opinion of value; an opinion of value.

Appreciation: An increase in the value of an asset over time. The increase can occur for a number of reasons including increased demand or weakening supply, or as a result of changes in inflation or interest rates. This is the opposite of depreciation, which is a decrease over time.

Assessed Value: The dollar value assigned to a property for purposes of measuring applicable taxes.

Comparable: A recently sold property, similar to the Subject property, used when determining value through the Sales Comparison Approach

Conventional Loan: A conventional mortgage refers to a loan that is not insured or guaranteed by the federal government. A conventional, or conforming, mortgage adheres to the guidelines set by Fannie Mae and Freddie Mac. It may have either a fixed or adjustable rate.

Cost Approach: A real estate valuation method that surmises that the price someone should pay for a piece of property should not exceed what someone would have to pay to build an equivalent building. In cost approach pricing, the market price for the property is equivalent to the cost of land plus cost of construction, less depreciation. It is often most accurate for market value when the property is new.

Depreciation: A reduction in the value of a property over time.

External Obsolescence: A type of depreciation or loss of value caused by negative influences outside the site and are beyond the control of the current property owner.

Fannie Mae: Federal National Mortgage Association – FNMA – A government-sponsored enterprise (GSE) that was created in 1938 to expand the flow of mortgage money by creating a secondary mortgage market. Fannie Mae is a publicly traded company which operates under a congressional charter that directs Fannie Mae to channel its efforts into increasing the availability and affordability of homeownership for low-, moderate- and middle-income Americans.

FHA: Federal Housing Administration – provides mortgage insurance on loans made by FHA-approved lenders throughout the United States and its territories. FHA insures mortgages on single family and multifamily homes including manufactured homes and hospitals.

Freddie Mac: Federal Home Loan Mortgage Corp – FHLMC – A stockholder-owned, government-sponsored enterprise (GSE) chartered by Congress in 1970 to keep money flowing to mortgage lenders in support of homeownership and rental housing for middle income Americans. The FHLMC purchases, guarantees and securitizes mortgages to form mortgage-backed securities. The mortgage-backed securities that it issues tend to be very liquid and carry a credit rating close to that of U.S. Treasuries.

Functional Obsolescence: A reduction in the usefulness or desirability of a property because of an outdated design feature, usually one that cannot be easily changed.

GLA: Gross Living Area – The ANSI standards define "finished area" as "an enclosed area in a house suitable for year-round use, embodying walls, floors, and ceilings that are similar to the rest of the house." Measurements must be taken to the nearest inch or tenth of a foot, and floor area must be reported to the nearest square foot. Garages are specifically excluded.

HUD: Housing and Urban Development – a cabinet of the United States federal government. It has existed since 1965 and is charged with ensuring smooth policy for housing and city development. Since the mid-1970s, its focus has shifted primarily to housing, leaving urban planning more in the hands of individual cities.

Market Value: A type of value, stated as an opinion, that presumes the transfer of a property (i.e., a right of ownership or a bundle of such rights), as of a certain date, under specific conditions set forth in the definition of the term identified by the appraiser as applicable in an appraisal.

MLS: A Multiple Listing Service, or MLS, is a marketing database set up by a group of cooperating real estate brokers. Its purpose is to provide accurate and structured data about properties for sale.

Site Value: The value of the Subject site as if vacant with no improvements. This is typically determined by using vacant land sales in the Subject's area similar in size, zoning and utility.

UAD: Uniform Appraisal Dataset is a component of the Uniform Mortgage Data Program, an initiative undertaken by Fannie Mae and Freddie Mac under the direction of the Federal Housing Finance Agency in the United States in order to comprehensively standardize mortgage loan data so that loans may be processed more efficiently.

Underwriting: The process a lender uses to determine if the risk of offering a mortgage loan to a particular borrower under certain parameters is acceptable.

USPAP: Uniform Standards of Professional Appraisal Practice – Develops requirements for appraisers considered to be the quality control standards applicable for real property, personal property, intangibles, and business valuation appraisal analysis and reports in the United States and its territories. The purpose of the USPAP is to promote and maintain a high level of public trust in appraisal practice by establishing requirements for appraisers.

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We hope you now understand a little more about how the appraised value of your property was arrived at, and that you have gained some appreciation for what a complex process **developing** an appraisal really is!

At NAN we strive to make everything easier for our Lenders so they can make it easier for you, the Borrower.

We ensure that all our processes are **SIMPLE**, our technology is **SMART** and our compliance is **SOLID**!

Nationwide
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