

# A GUIDE TO UNDERSTANDING A RESIDENTIAL APPRAISAL



THE APPRAISAL FOUNDATION

*Authorized by Congress as the Source of Appraisal  
Standards and Appraiser Qualifications*

Dear Consumer,

The purpose of this brochure is to help you understand the residential appraisal. After reviewing this brochure, you will understand the definition of a credible appraisal, the appraisal process, elements of a credible appraisal, the importance of appraiser independence, and how to proceed if you feel that a correction needs to be made to your appraisal report.

You may have recently entered into an agreement to purchase a residential property or you may have completed a loan application to refinance your home. Lenders are required to obtain an appraisal, prepared by an impartial and unbiased appraiser, and use it as the primary tool for assessing the sufficiency of your collateral. You may want to retain an appraiser to provide an appraisal to help you make decisions such as buying, selling or financing your home.

This brochure was produced by The Appraisal Foundation. The Appraisal Foundation is authorized by Congress as the source of appraisal standards and appraiser qualifications. You can obtain additional information about The Appraisal Foundation and the various boards that operate under its oversight at [www.appraisalfoundation.org](http://www.appraisalfoundation.org).

Sincerely,

The Appraisal Foundation

# THE PROCESS OF OBTAINING THE APPRAISAL

An appraisal is an opinion of value. For estate planning, financial planning, or sale price decisions, individuals or a trusted advisor usually orders an appraisal. When an appraisal is used to obtain an opinion of value of a property for loan purposes, federal regulation requires the lender or its agent to place an appraisal order. The lender or its agent contacts a state licensed or certified appraiser and identifies the property to be appraised and the intended use of the appraisal. The appraiser then determines the appropriate scope of work for the assignment.

The appraiser's scope of work typically includes the type of property inspection (interior, exterior only or none), what approaches to value are required, and any lender-specific requirements. In some cases, the lender may order the appraisal through an agent, such as an Appraisal Management Company (AMC).

There is no single standard appraisal report form, format, or style. However, for residential mortgage lending, Fannie Mae (FNMA) and Freddie Mac (FHLMC), which are Government Sponsored Enterprises (GSEs) that purchase mortgages on the secondary market, have developed residential appraisal report forms that are commonly used to communicate the appraisal of properties used as collateral. Regardless of the type of appraisal report used, all appraisal reports must contain sufficient information to enable the intended users to understand the report properly.



## THE APPRAISAL PROCESS

- If an appraisal requires an interior inspection, an appraiser will contact the homeowner (or, in the case of a sale, an agent or the seller) to inspect the interior and exterior of a property. As previously mentioned, an appraisal may not require an interior inspection.
- An appraiser will research county and municipal records, Multiple Listing Service (MLS) records, and other data services for information and documentation concerning the subject property and market area.
- An appraiser will review recent sales and listings of comparable properties. Comparables are recently sold or listed properties that have similar utility, quality, age and amenities as the subject property and are located in the subject property's market area. In markets where few sales have recently occurred, comparables may be from similar or competing neighborhoods located some distance from the subject property.
- An appraiser may use the *sales comparison approach* to develop an opinion of value. Often the primary approach to develop an opinion of value for a residential property, the *sales comparison approach* utilizes recent sales of comparable properties. An appraiser will analyze and compare characteristics that include the living area of the home, land area, style, age, quality of construction, number of bedrooms and bathrooms, presence or absence of a garage, etc.
- The *cost approach* is another method an appraiser may use to develop an opinion of value. The *cost approach* is the appraiser's opinion of the current replacement cost of constructing a reproduction of the existing structure, less any estimated depreciation, plus the value of the land. The *cost approach* is a valuable approach to use when appraising newer homes that might have little or no depreciation.
- Lastly, an appraiser may utilize the *income approach*. The *income approach* is most often used in appraisals of properties that have two, three or four living units, where income is a factor in the decision-making process of buyers and sellers. It is generally not used for one-unit residential properties in areas where the majority of the homes are owner-occupied.



- After data collection and analysis, the appraiser will develop an opinion of value by considering the indicated value(s) of the *sales comparison approach*, as well as the *cost approach* and/or *income approach*, if applicable. The values indicated by the approaches utilized will be reconciled to a final opinion of value. The appraiser will present his or her findings and conclusions in a report to the lender.



## ESSENTIAL ELEMENTS OF CREDIBLE APPRAISAL

Credible appraisals clearly identify the property appraised, the scope of work performed by the appraiser, the client and other intended users, and the intended use of the report. The appraisal report must include the definition of value (e.g., market value), the effective date of value, the subject property's relevant characteristics, and any other special instructions from the lender, Fannie Mae, Freddie Mac, VA, FHA, etc. A credible appraisal must effectively communicate the data and analysis required to support the opinion of value.

A credible appraisal must comply with the *Uniform Standards of Professional Appraisal Practice* and all regulatory requirements including the Federal Fair Housing Act, ECOA, as well as client-specific requirements.

## THE IMPORTANCE OF APPRAISER INDEPENDENCE

Appraisers are trained to deflect any attempt to influence the appraisal or value opinion, remaining independent, impartial and objective. The appraiser has the sole responsibility for the analyses, opinions, and conclusions contained in the appraisal.

Appraiser independence is a critical element to protect the client and intended users and to enhance the public trust that appraisals contain credible opinions of value. Furthermore, both Federal and State law requires appraiser independence. Without public trust, mortgage investors could withdraw funds from the market resulting in a shortage of funds for residential lending.

## WHAT TO DO IF IT IS DISCOVERED THAT A CORRECTION IS NECESSARY OR OTHER RELEVANT DATA SHOULD BE CONSIDERED

After reviewing your appraisal, if you believe the appraiser did not consider important information about the subject property or available comparables, discuss the matter with your lender. Submit your concerns in writing to the lender with a request that the appraiser be asked to address them. The appraiser should review the appraisal and, if additional credible information is pertinent to the appraisal assignment, provide a revised appraisal with commentary addressing your concerns.



## **WHAT TO DO IF THERE IS FRAUDULENT OR INCOMPETENT APPRAISAL PRACTICE**

If you suspect fraudulent or incompetent appraisal practice, submit your concerns in writing to the lender. Also, you may consider filing a complaint with the state appraiser regulatory agency in the state in which the property is located. The contact information for each state is available at [www.asc.gov](http://www.asc.gov). You may also contact the Financial Fraud Enforcement Task Force at [www.stopfraud.gov](http://www.stopfraud.gov).

Please be advised that state appraiser regulatory agencies will generally not act as a resource to you in trying to resolve any issues with the appraisal that may affect your transaction. Instead, the agency will consider your complaint in light of the appraiser's responsibilities under the law, and may take disciplinary action against the appraiser, if necessary.

## IMPORTANT TERMINOLOGY

**Appraisal** – An opinion of value.

**The Appraisal Foundation** - The Appraisal Foundation is a Congressionally authorized non-profit organization established in 1987. The Appraisal Foundation is dedicated to the advancement of the appraisal profession. The Foundation accomplishes its mission through the work of its three independent boards: the Appraisal Practices Board (APB), the Appraiser Qualifications Board (AQB) and the Appraisal Standards Board (ASB).

**Appraisal Management Company** – Appraisal Management Companies have contracts with companies (such as lenders) that require appraisal services. Appraisal Management Companies act as agents to hire the appraiser and provide other valuation services.

**Appraisal Practices Board (APB)** – The APB is charged with the responsibility of identifying and issuing opinions on recognized valuation methods and techniques, which may apply to all disciplines within the appraisal profession. Compliance with guidance issued by the APB is voluntary.

**Appraisal Review** – The act or process of developing and communicating an opinion about the quality of another appraiser’s work.

**Appraisal Standards Board (ASB)** – The ASB sets forth the rules for ethics and competency in developing an appraisal and reporting its results within the *Uniform Standards of Professional Appraisal Practice (USPAP)*.

**Appraiser Qualifications Board (AQB)** – The AQB establishes the minimum qualification criteria for state licensing, certification and recertification of real property appraisers.





**Comparable** – A shortened term for similar property sales, used for comparison in the valuation process; also called “comps.”

**Cost Approach** – A set of procedures through which a value is derived for a property by estimating the current cost to construct a reproduction of (or replacement for) the existing structure. This estimate includes deducting depreciation from the total cost, and adding the estimated land value.

**Credible appraisal** – A credible appraisal is one that is worthy of belief. A credible appraisal provides support, by relevant evidence and logic, for the opinion of value.

**Income Approach** – A set of procedures through which an appraiser derives a value for an income-producing property by converting its anticipated cash flows into property value.

**Licensed and Certified Appraisers** – Appraisers are licensed and certified by the state appraiser regulatory agencies, after meeting minimum education, experience and examination requirements. All states must adhere to, at a minimum, the criteria established by the Appraiser Qualifications Board of The Appraisal Foundation.

**Multiple Listing Service** – Typically the Multiple Listing Service is operated by the local/regional REALTORS® Associations and contains property listings, sales and expired listings. Most Licensed and Certified Appraisers have access to this information.

**Public record data** – Public record data include local, state and federal records and documents concerning the subject property and comparables. For most residential properties, public records are maintained by the county or local municipality and include the registry of deeds, tax assessment information, and plat and survey records. Other records may include soil surveys, topography maps, zoning maps, etc.

**Sales Comparison Approach** – A set of procedures in which a value is derived by comparing the property being appraised to similar properties that have been sold recently, then making adjustments to the sale prices of the comparables based on their differences to the property being appraised.



## FREQUENTLY ASKED QUESTIONS

### **Why is an appraisal necessary?**

The lender orders the appraisal to obtain an accurate description of the property and an independent opinion of value. The lender uses the appraisal to document that the real estate is appropriate collateral and determine whether the value of the property is sufficient to support the lending decision.

### **Why isn't the consumer considered to be the client when he or she pays the appraisal fee?**

Federal banking regulations require the financial institution to be the client, regardless of who pays the fee.

### **How does the appraiser develop the value opinion?**

The appraiser researches market data, public records and talks with buyers, sellers and real estate brokers active in the market area. Data researched includes sales, leases, and current listings of similar properties. Other data include land sales and residential construction costs. After all factors affecting the value are considered, the appraiser develops an opinion of value and prepares an appraisal report.

## **I have heard about problems with appraisers traveling long distances to appraise homes? How far is too far?**

The issue isn't so much "distance" or "how far is too far," rather the question that should be asked, "Is an appraiser from outside of my area *competent* to appraise my property?" Some appraisers work in many geographic areas and are knowledgeable and competent in all of them. Other appraisers have a limited range in which they normally appraise and they may not have the data or the experience to be competent outside their local market.

## **What information should I provide to the appraiser?**

The more information the appraiser has about your property, the better he or she will be able to develop a credible result. The appraiser will be interested in knowing if there are any private agreements or restrictions, easements or rights of way, encroachments, "agreed to" arrangements with abutters (e.g., fences, walls) on the property, etc. The appraiser may ask about the property's title, sales and rental history, and occupancy. He or she might ask if the property is under a pending purchase and sales agreement or option and, if so, the details about the agreement or option. If the property sold in the past three years, the appraiser may ask about the details of the transfers. Finally, the appraiser may inquire about physical characteristics of the property, including any additions, permits, etc.

If you are hiring the appraiser directly, the appraiser will want to know what the intended use of the appraisal will be. (NOTE: If you are engaging the appraiser to prepare an appraisal for a federally-related transaction, you should know that the lender or the lender's agent is required to engage the appraiser).

## **What should the appraiser do when he or she inspects my home?**

Based on the client's intended use of the appraisal, the appraiser determines whether an interior and/or exterior inspection or no inspection is required. Under many circumstances, the lender will require a full viewing of the property including an exterior and interior inspection.

Assuming that a complete inspection is required, the appraiser inspects the site, site improvements, and building improvements. The appraiser considers the site's size, shape, topography, drainage, and any other attributes that may affect value. He or she views the site improvements (e.g., paving, fences and walls, landscaping) to determine their contribution of value to the property. Finally, the appraiser inspects any structures. Some of the items considered are building style, number of stories, size, number of rooms (including bedrooms and baths, etc). He or she observes the structure's condition as an aid to estimating depreciation. In addition, the appraiser considers the property as a whole, including the dwelling

and any other improvements as well as any visible encumbrances (e.g. power lines, encroachments). Finally, the appraiser considers the property in relation to the neighborhood.

An appraiser's inspection and a home inspection are different. An appraiser gathers information to develop a value opinion and a home inspector gathers information to identify construction features, structural integrity and any needed repairs.

### **What is a comparable sale or comparable listing?**

A comparable sale is a recent sale that is similar to the subject property in terms of physical and functional attributes and location. A comparable listing is a current listing that is similar to the subject property in terms of physical and functional attributes and location. Comparable sales and listings are used in the sales comparison approach. In most cases, the sales comparison approach is the most reliable indicator of value for a residential property because it most directly reflects the actions of buyers and sellers in the market.

### **Why does an appraiser make "adjustments"?**

In developing an opinion of the value of a property, an appraiser considers recent sales of similar properties. Generally speaking, the sales that are the most similar to the property being appraised are the best indicators of value. However, since rarely are two properties exactly the same, the appraiser must account for differences between the property that sold and the property being appraised. These differences are called "adjustments." Adjustments are added or subtracted from the sale prices of the comparables to indicated an adjusted sale price for the property being appraised.

### **In what circumstance would an appraiser use the *cost approach* and/or *sales comparison approach*?**

The *cost approach* is based on the premise that an informed purchaser would pay no more for the subject property than the cost of constructing a substitute property with the same utility. Differences between the *sales comparison approach* and the *cost approach* are particularly evident when the property being appraised involves older improvements where depreciation due to age and functional obsolescence are difficult to estimate, or when the improvements are relatively unique or specialized and there are few comparable properties. If completed correctly, under ideal circumstances the indicated value by the cost approach should be similar to the estimated value by the sales comparison approach.

## **The appraiser did not complete an income approach to value. Is that ok?**

In most cases, yes. The income approach is based on the relationship of anticipated benefits (dollar income) to value. The income approach in residential appraising generally consists of little more than a gross rent multiplier analysis (the sale price of a property divided by its income potential). The gross rent multiplier analysis is very reliable in markets where homes are rented and sold frequently. However, the income approach is not applicable when the property appraised is located in a neighborhood where most homes are owner-occupied.

## **What elements should a credible appraisal include?**

- A clear, accurate description of the subject property
- Sales that are the most recent and most comparable
- Comments that explain important issues in the appraisal
- An opinion of value supported by the analysis of the comparable sales





## **What should I do if I believe a correction is needed to the appraisal report?**

First, write a letter or email to the lender describing the problem and provide any evidence you have. For example, if the appraisal has an incorrect living area size for the subject property, provide factual evidence which supports your position. If you believe the appraiser selected comparables that were not the most comparable, submit a list of the comparables you would like him or her to consider. The lender will provide this information to the appraiser and request the appraiser to consider what's been submitted.

## **After asking for a reconsideration of value, the appraisal remains flawed. What are my options?**

You may request the lender order an appraisal review assignment or to order a second appraisal (keep in mind the lender is not *required* to do either). An appraisal review is completed by a different appraiser who will verify the facts and data in the appraisal, search for additional comparables and provide a conclusion as to whether the comparables used in the appraisal are the most comparable. If the review appraiser does not agree with the opinion of value in the original appraisal, he or she will complete a sales comparison approach and provide his or her own opinion of value.

## **The appraisal I am reading has codes describing elements such as condition, construction quality and location. How do I find out what they mean?**

At the request of the lender/client, the appraisal report may be prepared in compliance with the Uniform Appraisal Dataset (UAD) developed by Fannie Mae and Freddie Mac. The UAD requires the appraiser to use standardized responses that include specific formats, definitions, abbreviations, and acronyms. Look through the appraisal for the UAD Definitions Addendum. In most cases, the addendum will be in the appraisal. If not, either request it from the lender or access it online at <https://www.efanniemae.com/sf/lqi/umdp/pdf/uadappendixfieldreqs.pdf> pages 34 through 37.

## **Why doesn't The Appraisal Foundation enforce the *Uniform Standards of Professional Appraisal Practice (USPAP)*?**

The Appraisal Foundation is charged with establishing uniform standards for professional appraisal practice and appraiser qualifications. The Appraisal Foundation is *not* granted authority to enforce USPAP.

Formal enforcement of appraisal standards is provided by the state appraiser regulatory agencies. There are a total of 55 jurisdictions (including states and U.S. territories) that have enacted legislation that requires those who represent themselves as real property appraisers to be licensed or certified and comply with USPAP.

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