Appraisal FAQ's

Every year, countless people in the United States buy, sell or refinance their own slice of the American Dream. Most, if not all, of these transactions include a simple line item for an appraisal. It has become an understood and accepted part of a real estate transaction. "Let's bring in the expert and make sure we're not spending too much on this property."

But is this the only reason to get an appraisal? Are there other times when the services of a certified, licensed, **independent**, and unbiased real estate professional might come in handy?

- **PMI Removal**

  Private Mortgage Insurance or PMI is the supplemental insurance that many lenders ask home buyers to purchase when the amount being loaned is more than 80% of the value of the home. Very often, this additional payment is folded into the monthly mortgage payment and is quickly forgotten. This is unfortunate because PMI becomes unnecessary when the remaining balance of the loan - whether through market appreciation or principal paydown - dips below this 80% level. In fact, the United States Congress passed a law in 1998 (the Homeowners Protection Act of 1998) that requires lenders to remove the PMI payments when the loan-to-value ratio conditions have been met. Many appraisers offer a specific service for home owners that believe they have met the 80% loan-to-value metric. The costs of these services are very often recovered in just a few months of not paying the PMI.

- **Pre-Sale Decisions**

  Before someone decides to sell a home, there are several decisions to be made. First and foremost: "How much should it sell for?" But first there may be other equally important questions to ask: "Would it be better to paint the entire house first?" "Should I put in that third bathroom?" "Should I complete my kitchen remodel?" Many things which we do to our houses have an effect on their value. Unfortunately, not all of them have an equal effect. While a kitchen remodel may improve the appeal of a home, it may not add nearly enough to the value to justify the expense. Appraisers can step in and help make these decisions. Unlike a Realtor, an appraiser has no vested interest in what amount the house sells for. His fee is based on his efforts, not a percentage of the sales price. So seeking a professional appraisal can often help homeowners make the best decisions on investing in their homes and setting a fair sales price.

- **Estate Planning, Liquidation or Divorce**

  The loss of a loved one is a difficult time in life. Likewise, a divorce can be a particularly traumatic experience. Sadly, these events are often complicated by difficult decisions regarding the disposition of an estate. Unlike many wealthy individuals, the majority of Americans do not have dedicated estate planners or executors to handle these issues. Also, in most cases, a home or other real property makes up a disproportionate share of the total estate value. Here too, an appraiser can help. Often the first step in fairly disposing of an estate is to understand its market value. Where property is involved, the appraiser can help determine the market value. At this point, equitable arrangements can more easily be arrived at among disputing parties. Everyone walks away knowing they've received a fair deal. There are other uses for real estate appraisals. The highly-trained individuals behind these services are always looking for ways to put their expertise to work for home owners and the people who support them.

What is an appraisal?

An appraisal is a thought process leading to an opinion of value. This opinion or estimate is arrived at through a formal process that typically uses the three "common approaches to value". They are the Cost Approach - which is what it would cost to replace the improvements, less physical deterioration and other factors, plus the land value. There is the Sales Comparison Approach - which involves making a comparison to other similar, nearby properties which have recently sold. The Sales Comparison Approach is normally the most accurate and best indicator of value for a residential property. The third approach is the Income Approach, which is of most importance in appraising income producing properties - it involves estimating what an investor would pay based on the income produced by the property.

What does an appraiser do?

An appraiser provides a professional, unbiased opinion of market value, to be used in making real estate decisions. Appraisers present their formal analysis in appraisal reports.

Why would a person need a home appraisal?

There are many reasons to obtain an appraisal with the most common reason being real estate and mortgage transactions. Other reasons for ordering an appraisal include:

- To obtain a loan.
- To lower your tax burden.
- To establish the replacement cost of insurance.

- To contest high property taxes.
- To settle an estate.
- To provide a negotiating tool when purchasing real estate.
- To determine a reasonable price when selling real estate.
- To protect your rights in a condemnation case.
- Because a government agency such as the IRS requires it.
- If you are involved in a lawsuit.

What is the difference between an appraisal and a home inspection?

The appraiser is not a home inspector nor does he/she do a complete home inspection. An inspection is a third-party evaluation of the accessible structure and mechanical systems of a house, from the roof to the foundation. The standard home inspector's report will include an evaluation of the condition of the home's heating system, central air conditioning system (temperature permitting), interior plumbing and electrical systems; the roof, attic, and visible insulation; walls, ceilings, floors, windows and doors; the foundation, basement, and visible structure.

What is the difference between an Appraisal and a Comparative Market Analysis (CMA)?

Simply put, the difference is night and day. The CMA relies on vague market trends. The appraisal relies on specific, verifiable comparable sales. In addition, the appraisal looks at other factors like condition, location and construction costs. A CMA delivers a "ball park figure." An appraisal delivers a defensible and carefully documented opinion of value.

But the biggest difference is the person creating the report. A CMA is created by a real estate agent who may or may not have a true grasp of the market or valuation concepts. The appraisal is created by a licensed, certified professional who has made a career out of valuing properties. Further, the appraiser is an independent voice, with no vested interest in the value of a home, unlike the real estate agent, whose income is tied to the value of the home.

What does the appraisal report contain?

Each report must reflect a credible estimate of value and must identify the following:

- The client and other intended users.
- The intended use of the report.
- The purpose of the assignment.
- The type of value reported and the definition of the value reported.
- The effective date of the appraiser's opinions and conclusions.

- Relevant property characteristics, including location attributes, physical attributes, legal attributes, economic attributes, the real property interest valued, and Non real estate items included in the appraisal, such as personal property, including trade fixtures and intangible items.
- All known: easements, restrictions, encumbrances, leases, reservations, covenants, contracts, declarations, special assessments, ordinances, and other items of a similar nature.
- Division of interest, such as fractional interest, physical segment and partial holding.
- The scope of work used to complete the assignment.

After completing the report, what assurance is there that the value indicated is valid?

In communicating an appraisal report, each appraiser must ensure the following:
- That the information analysis utilized in the appraisal was appropriate.
- That significant errors of omission or commission were not committed individually or collectively.
- That appraisal services were not rendered in a careless or negligent manner.
- That a credible, supportable appraisal report was communicated.

Most states require that real estate appraisers are state licensed or certified. The state licensed or certified appraiser is trained to render an unbiased opinion based upon extensive education and experience requirements. To become licensed or certified, appraisers must fulfill rigorous education and experience requirements. In addition, appraisers must abide by a strict industry code of ethics and comply with national standards of practice for real estate appraisal. The rules for developing an appraisal and reporting its results are insured by enforcement of the Uniform Standards of Professional Appraisal Practice (USPAP).

How are appraisers certified?

Regulations regarding licensing and certification of Real Estate Appraisers vary from state to state. However, licensing and certification is most often associated with many hours of coursework, tests and practical experience. Once an appraiser is licensed, he or she is required to take continuing education courses in order to keep the license current.

Who do appraisers work for?

Typically, appraisers are employed by lenders to estimate the value of real estate involved in a loan transaction. Appraisers also provide opinions in litigation cases, tax matters and investment decisions.

Where does an appraiser get the information used to estimate value?

Gathering data is one of the primary roles of an appraiser. Data can be divided into Specific and General. Specific data is gathered from the home itself. Location, condition, amenities, size and other specific data are gathered by the appraiser during an inspection.

General data is gathered from a number of sources. Local Multiple Listing Services (MLS) provide data on recently sold homes that might be used as comparables. Tax records and other public documents verify actual sales prices in a market. Flood zone data is gathered from FEMA data outlets, such as a la mode's InterFlood product. And most importantly, the appraiser gathers general data from his or her past experience in creating appraisals for other properties in the same market.

Why do I need a professional appraisal?

Anytime the value of your home or other real property is being used to make a significant financial decision, an appraisal helps. If you're selling your home, an appraisal helps you set the most appropriate value. If you're buying, it makes sure you don't overpay. If you're engaged in an estate settlement or divorce, it ensures that property is divided fairly. A home is often the single, largest financial asset anybody owns. Knowing its true value means you can the right financial decisions.

What is "Market Value?"

Market value or fair market value is the most probable price that a property should bring (will sell for) in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby: (1) buyer and seller are typically motivated; (2) both parties are well informed or well advised; (3) a reasonable time is allowed for exposure to the open market; (4) payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and (5) the price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

Who Actually Owns the Appraisal Report?

In most real estate transactions, the appraisal is ordered by the lender. While the home buyer pays for the report as part of the closing costs, the lender retains the right to use the report or any information contained within. The home buyer is entitled to a copy of the report - it's usually included with all of the other closing documents - but is not entitled to use the report for any other purpose without permission from the lender.

The exception to this rule is when a home owner engages an appraiser directly. In these cases, the appraiser may stipulate how the appraisal can be used; for PMI removal, or estate planning or tax challenges, for example. If not stipulated otherwise, the home owner can use the appraisal for any purpose.

Which home renovations add the most to the price?

The answer to this is different depending upon the location of the home. Different markets value amenities differently. Adding a central air conditioner in Houston, Texas may add significant value, while putting one in a home located in Buffalo, New York might not have much impact.

As a rule, the most value returned from renovating a home comes in the kitchen. According to one national survey, kitchen remodels returned an average of 88% of the investment. In other words, a $10,000 kitchen remodeling project would add approximately $8,800 to the value of the home. Bathrooms were second, returning 85%.