What Homebuyers Should Know About Their

Appraisal

A Public Service of

Maryland Association of Appraisers, Inc.

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What Is an Appraisal?

An Appraisal is an estimate of the *market value* of a property – the <u>most likely</u> price that a typical buyer would pay for a property and what a typical seller would sell it for – as of a specific date.

- It is performed by an Appraiser – a person that everyone involved agrees will be competent and unbiased and independent.

- Appraiser should be Licensed or Certified by the Maryland State Commission of Real Estate Appraisers

- That means he or she has

    - Special <u>education</u>
    - At least 2 years experience <u>training</u> under a Certified Appraiser

Why Is an Appraisal Needed?

- Banking rules require it

    - It is protection for the lender
        - If a buyer doesn't pay back the mortgage loan, the bank or other lender will have to sell the house to get its money back. That lender wants to make sure, before the money is turned over to you, the buyer, that the house would sell for at least as much as they loaned on it – otherwise, they will lose their depositors' money.

    - It is protection for you, the buyer
        - You don't want to pay more for the house than it is worth!
        - *Be sure the contract you sign has a contingency clause that says that if you can't get the mortgage you want, you will not have to buy the house*

- Your lender will hire the appraiser from their approved list

- You, the buyer, normally pay for the appraisal – either to the lender when you apply for the mortgage loan, or directly to the appraiser when he or she comes out to look at the property
    - Typically $350 to $550, depending on geographic area

- You are entitled to a copy of the appraisal report from the lender – <u>be sure to ask for it!</u>

Inspection of the Property

- The appraiser looks at a property in the same way that a buyer would

- Appraisers are <u>not</u> home inspectors! For example, they
    - Will not take the furnace apart to check its insides
    - Can not say whether wiring and plumbing is good
    - Do not do a termite inspection
    - Can not determine whether cracks are serious
    - Can not tell whether mold is dangerous

- The appraiser should be expected to report only those deficiencies that are readily seen or otherwise has knowledge of – this is to alert the client to potential problems that may require further investigation by specialized, qualified professionals!

- A *Home Inspector* routinely inspects all those things and decides whether there is a problem that needs to be addressed – but does not address value.

How Is Property Value Estimated?

- The appraiser will usually estimate the value in at least two different ways, then compare the two answers:

    - *Sales Comparison*

        - Your property will be compared to others that have sold recently

    - *Replacement Cost*

        - How much would it cost to buy a vacant lot in a similar location and build this same house?

How Does the "Sales Comparison" Work?

- The appraiser finds at least 3 properties that have sold recently – usually within the past year
    - They should be similar to one you are buying
    - They should be from the same neighborhood – or one just like it
    - They should be ones that you would have considered buying!
    - If foreclosures and/or short sales are prevalent in that market area, the appraiser may decide to include them – but then must explain their use

- The sales price of each of those properties is then adjusted for differences between that house and the one you are buying, to find out how much that buyer would have paid for your house
  - Features of that "comparable property" that are considered to be <u>better</u> than yours result in a dollar amount being <u>subtracted</u> from its sales price
  - If they are considered to be <u>not as good</u>, then the adjustment is <u>added</u>

- The three Adjusted Sales Prices make a "range of value"
  - That range should be fairly small – no more than a few thousand dollars

- The appraiser then decides what the <u>most likely</u> market value of the property being appraised is (that is, what a typical buyer would be willing to pay) from within that range

- It is important to note that adjustments made in the analysis are not necessarily the same as the actual differences in cost, but rather the value given those features by the market – by typical buyers.

How Is Replacement Cost Figured?

- The appraiser calculates the cost to build that house today

- Then adds for any <u>additional</u> improvements to the lot itself, like a fence or driveway

- Then subtracts the <u>Depreciation</u>

  - Wear and tear, such as weathering and damage (*Physical Depreciation*)

  - Unusual or outdated features that most people don't want (*Functional Depreciation*)

  - Things nearby the house that make it worth less than others in the neighborhood, such as a gas station across the street (*External Depreciation*)

  - (The amount of depreciation is often reduced by the owners taking good care of the home, making needed repairs, and updating it periodically to provide more modern features and design, such as in the kitchen and baths.)

- Finally, the present value of the <u>land</u> is added, as indicated by recent market activity

- The total figure indicates the "replacement cost" of the property, and should be near the value indicated by the Sales Comparison

What If I Think There's Something Wrong?
(or if I have a question)

- Talk first to:
    - Your homebuying counselor
    - The Maryland Association of Appraisers, Inc (info@mdappraisers.org)

- If the property you are buying is in the City of Baltimore, you can discuss your concerns with
    - The Baltimore City Home Ownership Institute
    - The Community Law Center (www.communitylaw.org or 410 366-0922)
    - St. Ambrose Housing Aid Center (telephone 410-235-5770)
    - Centro de la Comunidad (telephone 410-675-8906)

- You can file a complaint with
    - the Maryland Commission of Real Estate Appraisers and Home Inspectors
    - the Maryland Real Estate Commission
    - The Maryland Division of Financial Regulation
    - (All three share a website: www.dllr.state.md.us)