

Mortgage Banking

C O L U M N S
VALUE JUDGMENTS



APPRAISING PROPERTY—TO PROTECT THE LENDER, **IT TAKES A PRO**

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THE LAST THING A MORTGAGE BANKER NEEDS is to lend too much money on a property, resulting in a loan-to-value (LTV) ratio that is greater than underwriting guidelines permit. For protection from this highly undesirable

set of circumstances, a lender needs a solid appraisal done by a trained and certified professional appraiser.

According to the Appraisal Guidelines used by Richmond, Virginia-based SunTrust Mortgage, "The safety and soundness of mortgage loans secured by real estate depends upon the adequacy of the underwriting supporting the transaction. . . . Appraisals are an essential component of the loan underwriting process because appraisal reports contain the estimates of collateral values."

The SunTrust Mortgage guidelines go on to state, "A real estate appraisal must convey in writing an independent, impartial opinion of value of a particular property and is the result of a complete appraisal assignment performed by a state licensed or certified appraiser . . . in compliance with Uniform Standards of Professional Appraisal Practice, or USPAP."

No doubt, the key to obtaining a reliable and credible third-party property valuation is the professional appraiser, a licensed and trained individual who keeps current on market trends and new laws. By investing in the reasonable cost to obtain the services of a professional appraiser, the property buyers and sellers realize significant benefits.

Most—if not all—mortgage lenders will require the applicant to pay an appraiser to determine the value of the

property being purchased. Not only does this allow the lender to know how much the property is worth to set a loan amount, but it also lets the borrower know if the home he or she is interested in buying is overpriced or underpriced.

Appraisals also help sellers list their properties accurately so they can be competitive in the market.

Required training and experience

In terms of professional training and experience, what does it take to become a "pro" as a property appraiser? In Maryland, to cite one state as an example, the Department of Labor, Licensing and Regulation (DLLR) requires a licensed real estate appraiser to have completed 150 hours of courses approved by the state Commission of Real Estate Appraisers and Home Inspectors, and to have compiled at least 2,000 hours of appraisal work experience over a period

of at least two calendar years.

In Maryland, there are three categories of licensed real estate appraisers:

■ Licensed real estate appraiser: May provide appraisal services in federally related transactions with 1) non-complex one-to-four-unit residential properties with a transaction value less than \$1 million; 2) complex one-to-four-unit residential properties having a transaction value of less than \$250,000; and 3) commercial properties having a transaction value of less than \$250,000.

■ Certified residential real estate appraiser: May provide appraisal services in federally related transactions with: 1) one-to-four-unit residential properties without regard to value or complexity; and 2) commercial properties having a transaction value of less than \$250,000.

■ Certified general real estate appraiser: May provide appraisal services in federally related transactions with all

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types of residential or commercial real property without regard to value or complexity.

While gaining the 2,000 hours of appraisal work experience needed to qualify for an appraisal license in Maryland, an appraiser trainee must work under the supervision of a supervising certified appraiser. Once an appraiser trainee has completed the required appraisal work experience, he or she must pass a rigorous licensing exam. In Maryland, the licensing exams for licensed real estate appraiser and certified residential real estate appraiser are four hours in duration. For certified general real estate appraiser, it's a six-hour exam.

Real estate appraisal methods

There are two primary appraisal methods for residential real estate:

■ **Sales comparison approach**—This appraisal method, also known as the market approach, involves comparing the property to a number of similar properties in the area that have sold recently, called "comparables." The appraiser will collect a variety of data on the comparables, including public records, sale prices, square footage, amenities, date of sale and more. The appraiser will then make adjustments for the differences between the subject property and the comparables. The basic idea behind this approach is that the buyer shouldn't pay more for a property that is comparable in value to a substitute property with similar amenities and features.

■ **Cost approach**—This is an appraisal method that is more commonly used on new properties and evaluates the property based on its reproduction cost. Basically, it is a value based on how much the house would cost to rebuild if it were destroyed. Then, the land value and depreciation of any improvements is calculated and integrated into the appraisal. While this method is a very useful approach when appraising newer properties, it is considerably less reliable for older homes. The cost approach is also widely used when appraising special-purpose properties such as churches, schools, fire stations and so on.

Ensuring reliability and credibility

Verification of data is a big issue when it comes to formulating a reliable and credible property valuation. Comparable

values obtained from the multiple listing service (MLS) or from real estate brokers or agents must be verified by contacting parties to the transaction including the buyer, seller and/or settlement attorney. At minimum, verification should be provided by one of these parties.

Sometimes the true value of the property may be entirely based in the land itself. Moreover, in certain instances, physical improvements to the property can be a liability when they create a tear-down situation. In these more complex situations, the appraiser needs to have an understanding of local zoning ordinances and may have to contact county or municipal zoning personnel to interpret zoning for a particular property.

Choosing an appraisal pro

Here is a checklist of the factors to consider in selecting a professional appraiser:

- Experience with the property type being appraised;
- Broad overall experience in residential and/or commercial real estate;
- Geographical experience in the local area;
- Availability within settlement and underwriting time constraints; and
- Most importantly, a reputation for consistency in providing reliable and credible arm's-length appraisals.

The bottom line

Fundamentally, a real estate appraisal is a trained professional's opinion of value. This arm's-length opinion must be based on research in appropriate market areas, assembly and analysis of information pertinent to a property, and the knowledge and experience and professional judgment of the appraiser.

In the final analysis, the hallmark of a true appraisal professional is the steadfastness to avoid being influenced by anything except the facts surrounding the subject property being appraised. Lenders and buyers should demand nothing less.

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