

Flowchart of the Real Estate Appraisal Process

1 Loan Application

Homebuyers, homeowners, or those seeking to build a home usually need financing and will apply for a mortgage loan (i.e., purchase, refinance, construction, home equity) with a lending institution. Typically, a loan officer, mortgage broker, or loan processor is assigned to collect applicant information and financials, obtain disclosures, order an appraisal, and get the loan to closing.

The purpose of the appraisal is to ensure the price one is paying for a home is fair, consider whether the value of the property is sufficient to provide collateral for the mortgage loan, or determine how much equity one has in a home for purposes of a refinance with cash out.

2 Appraisal Is Ordered

The lending institution orders an appraisal on the dwelling. The lender may require an external appraisal inspection only or both an internal and external appraisal inspection (this is not the same as an inspection of the safety and condition of the home that many homebuyers require as a condition of purchase). Lenders have established relationships with appraisers, appraisal firms, and/or appraisal management companies, but the appraiser should not be associated with the lender, seller, or borrower. It is the job of an appraiser to provide an impartial estimate of the market value of a dwelling.

3 Prior to Appraisal Inspection

Prior to conducting an inspection, a real estate appraiser will pull data on the subject property from the Multiple Listing Service (MLS), local public records, and other data sources. This data includes the size and type of home and its style, special features, and location.

4 Approach

Appraisers may use three approaches for estimating the value of the subject property. The most common method is the sales comparison approach, in which an appraiser selects appropriate comparable properties ("comps") and then makes adjustments to the value of the subject property based on differences between that property and the comps (usually three).

Appraisers may also use the cost approach, in which an appraiser estimates what it would cost to build or replace the property based on its size and local area construction costs, plus the cost of the land, minus depreciation.

The third approach is the income approach, used for income-generating property, in which an appraiser estimates value based on the income the property is expected to generate over a specified period, among other factors.

5 Selection of Comparable Properties

For the commonly used sales comparison approach, an appraiser will review recent sales and active/pending listings of comparable properties near the subject dwelling, within the last six months. Comps are selected for similarities to the subject dwelling's quality, condition, age, size, number of rooms, amenities, upgrades, and proximity. If comps are limited in the surrounding neighborhood or within the last six months, the distance and time frame for recent sales may be expanded by the appraiser. The selection of comps plays a critical role in the appraisal estimate of value.

6 Appraisal Inspection

During an appraisal inspection, an appraiser will take photos (exterior and interior, as required); measure the exterior of the home to determine the size; and make observations about the condition of the exterior, the size and condition of internal rooms, any upgrades or features (such as built-in cabinets), the size of the basement and whether any part of it is finished, whether HVAC is in working condition, etc.

7 Adjustments

In the sales comparison approach, an appraiser must account for differences between the comps and the subject dwelling. These differences are called adjustments, and any additions or subtractions to the value of the dwelling must be noted in the determination of the estimated value of the dwelling. Differences accounted for in the appraisal include lot size, quality, age, condition, square footage of living space, design, room count, upgrades, location, sales concessions, amenities, garages, view, and other features that positively or negatively affect the property value.

For example, if one of the comps has an extra bedroom and bathroom but is priced the same as the subject property, the estimated value of the subject dwelling will be decreased by an appropriate amount.

8 Dwelling Value

Most lenders require that an appraiser use the Uniform Residential Appraisal Report, which captures the information about the subject property and comps, and on which the adjustments are detailed. On this form, an appraiser lists the appraised value of the subject dwelling. This value is the appraiser's estimate of the price at which the subject dwelling would likely sell in a competitive and open market.

9 Appraisal Submission and Availability

The appraisal report may be submitted to an intermediary (if one was selected) for quality control or forwarded directly to the lender's underwriting department. The appraisal is an important piece of information used by the lender in making a loan decision. The appraisal will be provided to the buyer's agent. The Equal Credit Opportunity Act requires that lenders also send a copy of the appraisal to the homebuyer(s), regardless of the loan decision of the lender.

10 Review and Reconsideration

If homebuyers/homeowners believe the appraised value is incorrect, the buyers/owners may submit a request for a reconsideration of the value. The request may include supporting evidence that the value is incorrect, such as improper selection of the comps used for the appraisal.