

New FHA Appraisal Reporting Requirements

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I recently attended a seminar on HUD's new Appendix D – Valuation Protocol. Appendix D is part of the FHA Handbook 4150.2. The revised appendix provides specific instructions for completing appraisal report forms.

The appraisal reporting form to be used will depend on the property type that is being appraised. The appraiser must select the appropriate appraisal form for reporting an FHA appraisal from the following:

1. **Uniform Residential Appraisal Report** (Fannie Mae Form 1004 March 2005) – Required to report an appraisal of a one-unit property or a one-unit property with an accessory unit.
2. **Manufactured Home Appraisal Report** (Fannie Mae Form 1004C March 2005) – Required to report an appraisal of a one-unit manufactured home.
3. **Individual Condominium Unit Appraisal Report** (Fannie Mae Form 1073 March 2005) – Required to report an appraisal of a unit in a condominium project or a condominium unit in a planned unit development (PUD).
4. **Small Residential Income Property Appraisal Report** (Fannie Mae Form 1025) – Required to report an appraisal of a two- to four-unit property.

An appraisal performed for HUD/FHA purposes requires that all sections of the appraisal form be addressed. The appraiser must complete the form in a manner that clearly reflects the thoroughness of the investigation and analysis of the appraisal findings. The conclusions about the observed conditions of the property provide the rationale for the opinion of market value. The completed appraisal form utilized, together with the required exhibits, constitutes the reporting instrument to HUD for FHA insured mortgages.

The revised Appendix D is 139 pages long. FHA approved appraisers need to familiarize themselves with the many changes HUD has made to their reporting requirements. Either read through the new Appendix D, or take a seminar on the new material. Knowing that appraisers procrastinate on everything, (except their billing), I have compiled a lengthy list of some of the major changes I found while reading through this monster appendix. It would be nice if HUD created a similar list to help appraisers, but if you were to ask them about it they would tell you they have made a helpful list for us already. It's called Appendix D. Feel free to pass this list along to your clients. I think it would be especially helpful to processors and underwriters.

- The appraiser must note in the appraisal if any portion of the roof could not adequately be observed (state which area(s) were unobservable). Based on the information reported by the appraiser, the underwriter will determine whether or not a roofing inspection is required. This disclosure would also apply when the roof is snow covered.

- Lead based paint hazards could exist in any home built before January 1, 1978. Correction is required to all defective painted surfaces.
- Cosmetic repairs are not required; however, they are to be considered in the overall condition rating and valuation of the property. Examples of cosmetic repairs would include surface treatments, beautification or adornment not required for the preservation of the property.
- If the appraisal is being performed for a refinance, you must enter the word “Refi” in the sales comparison analysis on the subject’s sales price line.
- Time adjustments should be based on Contract Dates, not Closing Dates.
- HUD does not consider the MLS to be a verification source, only a data source. However, some MLS services do report sale transfer info. The MLSNI in the Chicago market for example has a link to County tax records that does report sale transfer info. You might want to include the Doc number if available.
- When reporting the lot size for the subject and comps, HUD wants the information reported in a square footage/acreage format. They don’t want you to type in the lot dimensions ie. 25 x 125.
- Vapor barriers are no longer required in crawl spaces.
- In the sales comparison analysis most software should be showing three lines for Above Grade Room Count Gross Living Area adjustments. HUD would like the first line to reflect bathroom adjustment, the second line to reflect room count adjustment and the third line to reflect GLA adjustment.
- In the sales comparison analysis on the Quality of Construction line enter good”, “average”, “fair”, etc. using the quality rating from your cost service subscription, or provider (Marshall and Swift for example).
- If you do not develop the Income Approach, you must enter “ND” or “Not Dev” on indicated value line in the Reconciliation Section. It stands for Not Developed.
- HUD no longer requires a Cost Approach on new construction or properties less than one year old. The only time HUD requires the cost approach is on unique properties, if the property has specialized improvements, if the property is a manufactured house, or if the client requests the cost approach.
- You no longer have to report the estimated monthly rent for the subject in the Income Approach. If you do not develop the Income Approach, you must put N/A in each blank field in this section.
- A 2-4 unit dwelling with an accessory unit is ineligible for FHA financing. Watch out for illegal units especially in the basement or attic.
- Termite inspections are no longer required on FHA appraisals. Inspections are required only when there is evidence of decay, pest infestation, suspicious damage or when it is customary to the area or required by state law. You would need to condition the appraisal as an extraordinary assumption if you call for a termite inspection.
- Examine the electrical system to ensure that there is no visible frayed wiring, or exposed wires in living areas and note if the amperage appears adequate for the property.

- Operate a representative number of lighting fixtures, switches and receptacles inside the house, garage and on the exterior walls and note any deficiencies. If the appliances present at the time of the inspection do not appear to be reasonable (undersized), determine if there is adequate amperage to run “standard” appliances, as per local code.
- The appraiser is not required to insert any tool, probe or testing device inside the panels or to dismantle any electrical device or control.
- Flush the toilets and turn on a representative number of faucets to determine that the plumbing system is intact, that it does not emit foul odors, that faucets function appropriately, that both cold and hot water run and that there is no readily observable evidence of leaks or structural damage under fixtures.
- Turn on several cold water faucets in the house to check water pressure and flow. Flushing a toilet at the same time will also reveal any weaknesses in water pressure. Make sure you use a cold water faucet and not a hot water faucet to check water pressure.
- If the property has a septic system, examine it for any signs of failure or surface evidence of malfunction.
- Required repairs will be limited to necessary requirements. Remember the three “S’s”, Safety, Security and Soundness.
- Typical conditions that would require further inspection or testing by qualified individuals or entities include: infestation – evidence of termites, inoperative or inadequate plumbing, heating or electrical systems, structural failure in framing members, leaking or worn-out roofs, cracked masonry or foundation damage and drainage problems.
- HUD’s intended use statement is a little different than Fannie Mae’s. You must include the following intended use statement on all FHA appraisals: **The intended user of this appraisal report is the lender/client and HUD/FHA.**
- Include a building sketch showing the Gross Living Area above grade, including all exterior dimensions of the house. Include patios, porches, garages, breezeways and other offsets. State “covered” or “uncovered” to indicate a roof or no roof (such as over a patio). An interior sketch showing rooms is only required for properties exhibiting functional obsolescence attributable to the floor plan.
- Subject photos must be taken of the front and rear at opposite angles to show all sides of the dwelling. Additional photos are required for any improvements with contributory value that are not captured in either the front or rear photograph. Street scene photo must include a portion of the subject site. If the subject property is proposed construction and the improvements have not been started, the appraiser should take a photograph that shows the grade of the vacant lot.
- Minor property conditions that no longer require automatic repair for existing properties include, but are not limited to:
 - Missing handrails
 - Cracked or damaged exit doors that are otherwise operable
 - Cracked window glass

- Defective paint surfaces in homes constructed post 1978
- Minor plumbing leaks (such as leaky faucets)
- Defective floor finish or covering (worn through the finish, badly soiled carpeting)
- Evidence of previous (non-active) Wood Destroying Insect/Organism damage where there is no evidence of unrepaired structural damage
- Rotten or worn out counter tops
- Damaged plaster, sheetrock or other wall and ceiling materials in homes constructed post-1978
- Poor workmanship
- Trip hazards (cracked or partially heaving sidewalks, poorly installed carpeting)
- Crawl space with debris and trash
- Lack of an all weather driveway surface
- Examples of property conditions that may represent a risk to the health and safety of the occupants or the soundness of the property for which FHA will continue to require automatic repair for **existing** properties include, but are not limited to:
 - Inadequate access/egress from bedrooms to exterior of home
 - Leaking or worn out roofs (if 3 or more layers of shingles on leaking or worn out roof, all existing shingles must be removed before re-roofing)
 - Evidence of structural problems (such as foundation damage caused by excessive settlement)
 - Defective paint surfaces in homes constructed pre-1978
 - Defective exterior paint surfaces in home constructed post-1978 where the finish is otherwise unprotected
- FHA no longer mandates automatic inspections for the following items and/or conditions in existing properties:
 - Wood Destroying Insects/Organisms
 - Well (individual water system)
 - Septic
 - Flat and/or unobservable roof

Inspections for these items would be necessary if the appraiser observed possible infestation, well and septic problems, water damage attributed to the roof, or if an inspection for these issues is mandated by state or local jurisdiction.
- If the property is less than one year old, included both the month and year completed.
- If the property is vacant, the appraiser should note, in the “Improvements” section under “condition of the property,” whether the utilities were on or off at the time of the appraisal. If off, condition the appraisal on a satisfactory re-inspection that the utility that was off at the time of the appraisal does not require alteration, repair or further inspection.
- If the current use of the property is determined to be illegal based on zoning, it would not be eligible for FHA mortgage insurance.

- Properties that are either Proposed or Under Construction require plans and specifications for the appraiser to review.
- An FHA appraisal may not be transmitted to the lender without a case number reported in the top right corner of the page.
- FHA requires the appraiser to report any prior listings of the subject property in the past 12 months. However, Illinois has a supplemental standard in our law that requires a 36 month listing history for the subject property for 1 to 4 family properties only. So you must perform a 36 month listing history.
- The crawl space must have either an interior or exterior access. The access to the crawl space should be clear. Examine the crawl space for inadequate access (minimum entry of the head and shoulders). Check the distance from the bottom of floor joists to ground. Space should be adequate for maintenance and repair. A minimum distance of 18 inches from the ground to the bottom of the joists is highly recommended **but not mandated**.
- Turn on the furnace/heating system to test functionality, weather permitting, and that no unusual noises are heard, no odors or smoke are emitted indicating a defective unit, etc. However, do not operate the systems if doing so may damage equipment or when outside temperatures will not allow system to operate. Disclose in the report that the outside temperatures would not allow testing of the system without possibly damaging the equipment.
- Turn on the air conditioning system to test functionality, weather permitting, and that no unusual noises are heard, no odors or smoke are emitted indicating a defective unit, etc. However, do not operate the systems if doing so may damage equipment or when outside temperatures will not allow system to operate. Disclose in the report that the outside temperatures would not allow testing of the system without possibly damaging the equipment.
- Bedroom windows with security bars require a quick release mechanism for emergency egress. If not so equipped or inoperable, condition the appraisal on a “required repair”.
- Enter the material type for the exterior walls: aluminum, vinyl or wood siding, brick veneer, stucco, stone, etc. If a combination of materials, show the predominant portion first and rate the observed condition. Ex: Brick/Frame/Average

Finally, there is a great definition on page D-7 of what an FHA appraisal is and is not. I would urge you all to copy and paste this into your reports.

FHA Appraisals

FHA appraisals are no guarantee that the property is free from defects. The appraisal only establishes the value of the property for mortgage insurance purposes. Buyers need to secure their own home inspections through the services of a qualified inspector and satisfy themselves about the condition of the property.