

CHAPTER 2

PROPERTY APPRAISAL AND VALUATION

2-1 PURPOSE OF THE APPRAISAL. The appraisal serves two main purposes:

- A. Condition/Location.** Appraisals determine eligibility for mortgage insurance based on the condition and location of the property.
- B. Value.** Appraisals estimate the value of the property for mortgage insurance purposes.

2-2 PROPERTY APPRAISAL AND UNDERWRITING PROCESS. **The property appraisal and underwriting process varies by the stage of construction and type of processing.**

FHA's appraisal handbook is 4150.2.

2-3 APPRAISAL REQUIREMENTS. Except for certain streamline refinance transactions, FHA requires an appraisal of the property to establish an estimated value for mortgage insurance purposes. All individual properties, whether proposed construction, under construction, or existing construction, must meet specific FHA appraisal requirements and standards.

See HUD Handbooks 4140.1, 4150.1, and 4150.2 for additional information about the appraisal requirements for individual properties.

Only one- to four-unit properties are eligible for mortgage insurance, except for mortgages insured under Section 220 of the National Housing Act. See Chapter 6 of this handbook for additional information on the Section 220 program.

2-4 APPRAISAL REPORTING REQUIREMENTS. An appraisal performed for FHA purposes requires the reporting of the three part Comprehensive Evaluation Package. Details on requirements for completion of this package are contained in HUD Handbook 4150.2. The Comprehensive Evaluation Package consists of the following:

- A. Uniform Residential Appraisal Report** – URAR (Fannie Mae Form 1004) is required. However, appraisals written on the Individual Condominium Unit Appraisal Report (Fannie Mae Form 1073) or the Small Residential Income Property Appraisal Report (Fannie Mae Form 1025) forms are also acceptable, as to applicable property types, to the Department for FHA-insured mortgages.
- B. Notice to the Lender** – **Valuation Conditions (Form HUD 92564-VC)**

C. **Notice to the Homebuyer – Homebuyer Summary**
(Form HUD 92564-HS).

2-5 **CONDOMINIUMS.** A condominium is a multi-unit project with individually owned units that may be attached in one or more structures, or detached from each other. Its use, for FHA purposes, is essentially residential. A condominium regime is created by state or local law and is characterized by fee simple ownership of a unit (as defined in the condominium documents), together with common areas. The property interest in these areas is both common and undivided on the part of all unit owners, each of whom belongs to the HOA that typically maintains the property and collects assessments or dues from each unit owner for that purpose. See HUD Handbooks 4150.1 and 4265.1 for additional information including condominium project approval requirements.

In addition, condominium projects must be approved by FHA before a mortgage on an individual condominium unit in the condominium project can be insured. In specific circumstances, a loan on a single unit in an unapproved condominium project, known as a “spot loan,” may qualify for mortgage insurance. The lender must certify that a project satisfies the eligibility criteria for a spot loan condominium project that has not been approved by FHA.

See HUD Handbooks 4150.2 and 4265.1 for additional information including condominium project approval requirements.

2-6 **GENERAL ACCEPTABILITY STANDARDS FOR PROPERTY.** There are minimum property standards for existing and proposed construction. A property is considered "existing construction" if it was completed more than one year prior to application. See HUD Handbooks 4905.1 and 4910.1 for additional information on existing and proposed construction, respectively.

Underwriters bear primary responsibility for determining eligibility of a property for FHA mortgage insurance. However, the FHA appraiser is the on-site representative for the Mortgagee and provides preliminary verification that these standards have been met. The “Notice to the Lender” requires the FHA appraiser to report the physical conditions that are readily observable on the date of the site visit and to detail the repairs needed to establish and/or maintain the marketability of the property, protect the health and safety of the occupants, and protect the security of the property. These criteria must be addressed by the Mortgagee before closing.

When examination of existing construction reveals noncompliance with the General Acceptability Criteria, an appropriate specific condition to correct the deficiency is required if correction is feasible. If correction is not feasible and only major repairs or alterations can effect compliance, the Mortgagee will reject the property.

The following is a general outline of the minimum property standards:

- A. **Eligible Houses.** Detached, semi-detached, row houses, multiplex and individual condominium dwellings are eligible. If it is not detached, the dwelling must be separated from an adjoining dwelling by a party or lot line wall extending the full height of the building. Each living unit must be individually accessible for use and maintenance without trespass on adjoining properties.
- B. **Eligible Manufactured Homes.** The following requirements apply to all manufactured homes:
1. At least 400 square feet minimum floor area
 2. Built after June 15, 1976, to the Federal Manufactured Home Construction and Safety Standards (MHCSS) as evidenced by an affixed certification label
 - a. 3. Property is classified and taxed as real estate and is designed to be used as a dwelling with a permanent foundation built to FHA requirements
 4. Built and remains on a permanent chassis
 5. Mortgage covers both the unit and its site, and has a term of not more than 30 years from date that amortization begins
 6. Finished grade beneath home is at or above the 100-year flood elevation

See HUD Handbooks 4145.1 and 4150.2 for additional information.

- C. **Site Conditions.** The property must be free of health and safety hazards.
- D. **Flood Hazard Areas.** The Mortgagee is responsible for determining the eligibility of properties in flood hazard areas and relies upon the FHA appraiser's notation on the URAR form.
1. **Proposed and New Construction.** If any portion of the property improvements (the dwelling and related structures/equipment essential to the value of the property and subject to flood damage) is located within a special flood hazard area (SFHA) designated by the Federal Emergency Management Agency (FEMA), the property is not eligible for FHA mortgage insurance unless: (1) a final Letter of Map Amendment (LOMA) or final Letter of Map

Revision (LOMR) that removed the property from the SFHA location is obtained from FEMA or (2) if the property is not removed from the SFHA location by a LOMA or LOMR, the lender obtains a FEMA National Flood Insurance Program Elevation Certificate (form FEMA 81-31) (“flood elevation certificate”) documenting that the lowest floor (including the basement) of the residential building and related improvements to the property is built at or above the 100 year flood elevation in compliance with the National Flood Insurance program criteria (see 44 CFR 60.3 through 60.6). National flood insurance is not required if a LOMA or LOMR is obtained but is required when a flood elevation certificate documents that the property remains located within the SFHA. The LOMA, LOMR, or flood elevation certificate must be submitted with the case for endorsement.

If the lender is uncertain about whether the property is located within a SFHA, it may require a flood elevation certificate. In addition, the lender has discretion to require national flood insurance even if the residential building and related improvements to the property are not located within the SFHA, but the lender has reason to believe that the building and related improvements to the property may be vulnerable to damage from flooding.

2. **Existing Construction.** Flood insurance must be obtained and maintained for an existing property with any portion of the residential buildings located in a special flood hazard area.
3. **Insurance Amount Required.** National flood insurance must be maintained in an amount equal to the least of the following: (1) the cost of the improved property (less estimated land costs); (2) the maximum limit of coverage made under the National Flood Insurance Act of 1968; or (3) the outstanding principal balance of the loan. Flood insurance is required for the term of the loan. If the buildings are located within a special flood hazard area (SFHA) and insurance under the National Flood Insurance Program is not available within a community, the property is not eligible for FHA mortgage insurance. See HUD Handbooks 4150.1 and 4150.2 for additional information.
4. **Condominium.** The Homeowners’ Association (HOA), not the individual owner, is responsible for maintaining flood insurance on buildings located within the special flood hazard area. If the FHA appraiser reports that buildings in a condominium project are located within a FEMA-designated SFHA, the lender is responsible for ensuring that the HOA obtains and maintains national flood insurance on buildings located within the SFHA.

The lender is not permitted to submit a LOMA, LOMR or elevation certification for any specific dwelling unit located within a newly constructed condominium project less than one year old.

5. **Manufactured Homes.** If any portion of the property improvements for both new and existing manufactured home properties are located within a SFHA, the property is not eligible for FHA mortgage insurance without: 1) a FEMA issued LOMA or LOMR, or 2) an elevation certification prepared by a licensed engineer or surveyor on the finished construction indication the ground beneath the manufactured home is at or above the 100 year flood plain. When utilizing an elevation certification, the property is still in the SFHA and the loan will require flood insurance.
- E. Lead-Based Paint Hazard.** If the property was built before 1978, the seller must disclose known information on lead-based paint and lead-based paint hazards before selling the house. Sales contracts must include a disclosure form about lead-based paint. Buyers have up to 10 days to check for lead. HUD may insure a mortgage on a house even with lead-based paint if defective paint surfaces are treated. HUD will not pay the cost to have the lead-based paint removed, treated, or repaired.
- F. Services and Facilities.** Utilities and other facilities should be independent for each unit and must include:
1. A continuing supply of safe, potable water
 2. Sanitary facilities and a safe method of sewage disposal
 3. Heating adequate for health and comfort
 4. Domestic hot water, and
 5. Electricity for lighting and equipment
- G. Access.** There must be vehicular access to the property by means of an abutting all-weather public or private street. If private, there must be a permanent easement and provisions for permanent maintenance. Each property must have access to its rear yard.
- H. Non-Residential Use.** Non-residential use must be subordinate to the property's residential use and character, and it may not exceed 25% of the total floor area. The following are ineligible for mortgage insurance:
1. Commercial enterprises

2. Boarding houses
3. Hotels/motels
4. Tourist houses
5. Private clubs
6. Bed and Breakfast establishments
7. Fraternity/sorority houses

2-7 USE OF VA CERTIFICATE OF REASONABLE VALUE (VA-MCRV). A Department of Veterans Affairs VA-CRV or a VA Notice of Value (NOV) form may be used as acceptable evidence of a property's eligibility, unless:

- A. Property has an outstanding FHA conditional commitment (HUD employees only)
- B. Property or site is known to be unacceptable (for example, subject to periodic flooding)
- C. Property or site was previously rejected by FHA
- D. The VA-MCRV or VA-NOV expired before the sales contract was signed
- E. Case is being processed under the DE program and property does not qualify as proposed construction. See HUD Handbook 4000.4, paragraph 1-2 for additional information on using a VA-MCRV in the DE program.
- F. Property is a unit in a condominium project that does not meet FHA criteria

The appraiser who performed the appraisal for the VA-MCRV or VA-NOV must currently be on the FHA appraiser roster. The HUD/FHA forms "Notice to the Lender" and "Notice to the Homebuyer" are also required.

2-8 REQUESTING AN FHA CASE NUMBER. Lenders request and obtain FHA case numbers using FHA Connection or its functional equivalent. Any additional FHA information on the property will also be transmitted over the FHA Connection.

2-9 TERM OF APPRAISAL.

- A. Term.** The appraisal has a term of six months for existing construction and 12 months for proposed construction. However, if the appropriate HOC determines that soft market conditions exist in certain areas or markets, it may shorten the term of appraisals for proposed construction and substantial rehabilitation to a period of less than 12 months upon advance notice to lenders. The term of the appraisal begins on the day the home is inspected by the FHA appraiser and this date appears on the URAR.
- B. Re-Use.** Appraisals cannot be re-used after the mortgage for which the appraisal was ordered has closed. For example, an appraisal used for the purchase of a property cannot be used again for a subsequent refinance, even if six months has not passed. A new appraisal is required for each refinance transaction requiring an appraisal.
- C. Extensions.** If a borrower signs a valid sales contract or is approved for a loan prior to the expiration date of the appraisal, the term of the appraisal may be extended, at the option of the lender, for 30 days to allow for the approval of the borrower and closing of the loan. Approval of the borrower occurs when the lender's DE underwriter signs the Mortgage Credit Analysis Worksheet, Form HUD-92900-WS/92900-PUR.

2-10 COMPLIANCE INSPECTIONS. Compliance inspections may be required for:

- A.** Proposed construction or properties under construction
- B.** Properties undergoing substantial rehabilitation, and
- C.** Existing properties requiring repairs to major systems (structural, etc.).

The number and timing of inspections depends upon the stage of construction (proposed, rehabilitation, etc.), coverage by an acceptable 10-year warranty plan, acceptability of inspections by the local community, and the type of construction (stick built or manufactured home). A clear final inspection or, in certain cases, a Certificate of Occupancy will be required before FHA will insure the mortgage. See HUD Handbooks 4145.1, 4150.1 and 4150.2 for additional information.

2-11 SATISFYING REPAIR REQUIREMENTS. Repair requirements outstanding on the appraisal report must be satisfied before the mortgage is submitted for endorsement. Satisfaction of repair requirements can take one of the following three forms.

- A. **Compliance Inspection Report (Form HUD-92051).** A Compliance Inspection Report, prepared by an appraiser or inspector, certifies that the repairs have been completed satisfactorily.

Generally, since an appraiser places the repair requirements, the same appraiser would be able to determine whether the repair has been made. For inspections that require architectural expertise (structural or basic system repairs), an inspector must complete Form HUD-92051. A FHA fee inspector must complete the report. A FHA-approved inspector list is available via FHA Connection located at <https://entp.hud.gov/clas/>. In addition to the appraiser or inspector, a professionally licensed, bonded, registered engineer, licensed home inspector or appropriately registered/licensed trades person, as applicable, can provide the documentation to support that all deficiencies noted by the FHA appraiser have been acceptably corrected. The report must be reviewed by FHA or the lender's underwriter, as appropriate.

- B. **Mortgagee Certification.** Mortgagee certification (that the conditions have been satisfied) is acceptable in instances in which the required repair items are minor and uncomplicated. If the homeowner could complete the work himself or herself as normal maintenance, FHA considers the work minor.

- C. **Escrow of Funds.** If adverse weather conditions prevent completion of the repairs, it is not always necessary to complete all new construction items (for example, landscaping) or required repairs (such as exterior painting) before submitting the mortgage for insurance endorsement. In certain situations, funds may be escrowed, and FHA will accept a Mortgagee's Assurance of Completion, Form HUD-92300, at the time of endorsement.

This procedure may be used only when the following conditions apply:

1. The dwelling is habitable, safe, and essentially complete
2. The deferred work cannot be acceptably completed prior to loan closing, but will be completed within six months
3. All other conditions of the appraisal have been satisfied by compliance inspections or by an acceptable Mortgagee's Assurance of Completion, and
4. The lender has not been denied the privilege of using a Mortgagee's Assurance of Completion due to poor follow-up or non-satisfaction of outstanding escrows

The lender assumes the obligation to satisfactorily complete the improvements, regardless of the adequacy of the funds reserved by escrow or letter of credit. An appraiser or an inspector appearing on FHA's Appraiser Roster or FHA's Panel of Inspectors must confirm that the work was completed. Lists of these individuals are located on HUD's Web site at www.hud.gov. Alternately, as mentioned in paragraph 2-12A of this handbook, a professionally licensed, bonded, registered engineer; licensed home inspector; or appropriately registered/licensed trades person, as applicable, can provide the documentation to support that all deficiencies noted by the appraiser been acceptably corrected.

See HUD Handbook 4145.1 for additional information on this procedure.

- 2-12** **SECTION 223(e).** A mortgage may be insured pursuant to Section 223(e) for the repair, rehabilitation, construction, or purchase of properties in older, declining urban areas. Eligibility under Section 223(e) is to be determined by the appropriate HOC.

If the case is being processed under DE, the lender must submit the case binder to the appropriate HOC for prior approval processing and 223(e) consideration. The case binder must be submitted after the appraiser and the lender's underwriter have determined that the property does not meet the location eligibility requirements of Section 203(b), but is located in an older, declining urban area that may qualify for 223(e). See Chapter 6 of this handbook for additional information.

- 2-13** **APPRAISAL AND INSPECTION FEES.** The lender is responsible for collecting fees and promptly paying appraisers and inspectors.

- 2-14** **DOCUMENTATION OF APPRAISED VALUE.** In accordance with the provisions of the National Housing Act, the lender must provide to the homebuyer a Statement of Appraised Value. The lender accomplishes this requirement by giving the borrower a copy of Form HUD-92800.5B. When a VA-MCRV issued by the VA or a NOV issued by a lender in accordance with VA requirements is the basis for the estimate of the appraised value, the lender must provide a copy of the VA-MCRV or NOV to the borrower. If the borrower requests a copy of the appraisal, the lender must provide it to the borrower.