Bankers Advisory
COMPLIANCE MONITOR

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Fannie Mae Updates Appraisal Underwriting Rules

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February 4, 2015, Fannie Mae published Lender Letter LL-2015-02: Appraisal Tools, Processes and Policies. The purpose of the Lender Letter is to provide clarifications and additional information regarding Fannie Mae's valuation-related tools and policy updates announced within the past 12 to 18 months. These include Collateral Underwriter™ (CU™), Appraiser Quality Monitoring (AQM), and updates to the Property Eligibility and Appraisal Requirements section of the Selling Guide.

This article highlights the updates to property eligibility and revisions to the Selling Guide. Please refer to the previous ***Compliance Monitor*** article regarding Fannie Mae's Collateral Underwriter and Appraiser Quality Monitoring.

Summary of Selling Guide Policy Updates

Adjustments to Comparable Sales

In the December, 2014 Selling Guide update, Fannie Mae removed a long-standing guideline that when adjustments to the comparable sales exceeded 15% net and 25% gross, the appraiser was required to provide an explanation as to why the comparable was chosen for use in the appraisal report. The requirement for commentary was based on the premise that the best comparable would require the fewest adjustments.

While the premise remains true in theory, the guideline for 15% net and 25% adjustments was widely implemented as an eligibility "hard stop" due to many rules-based automated review systems. Analysis of appraisals submitted to UCDP made it clear that many appraisal reports never exceeded the 15% or 25% guideline – the focus of many appraisers had become keeping the amount of the adjustments within the guidelines instead of reflecting actual market reaction for specific characteristic(s).

The analysis results reflected in the charts provide strong evidence that adjustments have been made to fit within guidelines that were not intended to be rules, but instead a trigger for commentary and rationale. While the best comps remain those that warrant lower adjustments – if those adjustments are based on market reaction and well-supported – the removal of the net and gross adjustment guidelines appropriately shifts focus to supporting market-based adjustments regardless of the amount of the adjustment either as a single line item or in total. Another point of clarification is that Fannie Mae currently does not have, and has never had, a limitation on a single-line item adjustment.

Photographs

In 2010, Fannie Mae added a requirement for appraisals to include interior photographs of specific rooms and examples of deterioration or updating if present within the property. This was in addition to the previous requirements for clear and descriptive photographs of the front, rear, and street scene of the subject property as well as photographs of the front of the comparable sales.

As a clarification, Fannie Mae requires the lender to ensure that all photographs in the appraisal report are clear and descriptive. Photographs that are out of focus or taken with improper light, rendering them not clear and descriptive, are not acceptable. Lenders should remind appraisers to use a flash in dark areas and review images to ensure they are not blurry. The purpose of this requirement is to enable all parties relying on the report to be able to clearly identify the property's condition and quality.

Condition Ratings

The Uniform Appraisal Dataset (UAD) includes definitions for Condition Ratings C1 – C6. Fannie Mae will accept loans secured by properties with any condition rating (provided all other requirements are met), except that a C6 rating must be "subject to" and subsequently reflect the condition rating of the repaired property.

It is important to note that loans secured by properties with C5 condition ratings are deliverable to Fannie Mae with "as-is" reports, provided the property meets the following C5 definition:

"The improvements feature obvious deferred maintenance and are in need of some significant repairs. Some building components need repairs, rehabilitation, or updating. The functional utility and overall livability are somewhat diminished due to condition, but the dwelling remains useable and functional as a residence."

Note: Some significant repairs are needed to the improvements due to the lack of adequate maintenance. It reflects a property in which many of its short-lived building components are at the end of or have exceeded their physical life expectancy, but remain functional.

Selection of Comparable Sales

Fannie Mae no longer requires specific comments from an appraiser if a comparable sale is older than 6 months; however, a comment is still required when a comparable sale is older than 12 months. The expectation is for comparable sales to have closed within the past 12 months and be the best and most appropriate. However, there are times when the best and most appropriate comparable sales are not the most recent sales. It may be appropriate for the appraiser to use a 9-month-old sale with a time adjustment rather than a 1-month-old sale that requires multiple adjustments. Older sales may be more appropriate in situations when market conditions have impacted the availability of recent sales, as long as the appraisal reflects the changing market conditions.

Older comparable sales (including sales older than 12 months) that are the best indicator of value for the subject property can be used if appropriate. For example, if the subject property is located in a rural area that has minimal sales activity, the appraiser may not be able to locate 3 truly comparable sales that sold in the past 12 months. In this case, the appraiser may use older comparable sales as long as he or she explains why they are being used.

Please refer to the materials published on the Fannie Mae website for additional important information and supportive data and charts.