



Selling Guide

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B4-1.3-03: Neighborhood Section of the Appraisal Report (09/30/2014)

This topic contains information on reviewing the Neighborhood section of the appraisal report form, including:

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Overview

Neighborhood characteristics and trends influence the value of one- to four-unit residences. Therefore, an analysis of the subject property's neighborhood is a key element in the appraisal process. As a reminder, Fannie Mae purchases mortgages secured by properties in all neighborhoods and in all areas, as long as the property is acceptable as security for the mortgage based on its value and marketability.

Neighborhood Analysis

Fannie Mae's appraisal report forms and guidelines do not require the appraiser to rate or judge the neighborhood. Fannie Mae requires the appraiser to perform an objective neighborhood analysis by identifying neighborhood boundaries, neighborhood characteristics, and the factors that affect the value and marketability of properties in the neighborhood.

- **Neighborhood boundaries.** The appraiser should provide an outline of the neighborhood boundaries, which should be clearly delineated using 'North', 'South', 'East', and 'West'. These boundaries may include, but are not limited to streets, legally recognized neighborhood boundaries, waterways, or other natural boundaries that define the separation of one neighborhood from another. Appraisers should not reference a map or other addendum as the only example of the neighborhood boundaries.
- **Neighborhood characteristics.** These can be addressed by the types of structures (detached, attached) and architectural styles in the neighborhood (such as row or townhouse, colonial, ranch, or Victorian); current land use (such as single-family residential, commercial, or industrial); typical site size (such as 10000 sf, or 2.00 ac); or street patterns or design (such as one-way street, cul-de-sac, or court).
- **Factors that affect the value and marketability of properties in the neighborhood.** These can be addressed by such things as the proximity of the property to employment and amenities, employment stability, appeal to the market, changes in land use, access to public transportation, and adverse environmental influences.

The appraiser must fully consider all of the value-influencing characteristics in the neighborhood and arrive at an appropriate neighborhood description and opinion of value for the property, even if this requires more extensive research for particular property types or for properties in certain geographic locations.

An appraiser must perform a neighborhood analysis in order to identify the area that is subject to the same influences as the property being appraised, based on the actions of typical buyers. The results of a neighborhood analysis enable the appraiser not only to identify the factors that influence the value of properties in the neighborhood, but also to define the area from which to select the market data needed to perform a sales comparison analysis.

In performing a neighborhood analysis, the appraiser

- collects pertinent data,
- conducts a visual inspection of the neighborhood to observe its physical characteristics and determine its boundaries, and
- identifies land uses and any signs that the land uses are changing.

Fannie Mae expects the appraiser and the lender's underwriter to be aware of the varying conditions that characterize different types of neighborhoods. Conditions that are typical in certain neighborhoods may not be present in other neighborhoods. This does not mean that the existence of certain types of conditions or characteristics are unacceptable; rather, it is an indication that they must be viewed in context with the nature of the neighborhood in which the security property is located. For example, some neighborhoods consist of a variety of property types that have different uses. It is not uncommon to find properties that have mixed-uses, such as residential properties that also have child-care facilities, doctor or dental offices, and other types of business or commercial uses. The presence of mixed-use properties or a variety of property types within a neighborhood should be viewed as a neighborhood characteristic that the appraiser considers when performing the neighborhood analysis and describing the neighborhood boundaries.

The appraiser must consider the influence of market forces, including but not limited to, economic, governmental, and environmental factors on property values in the neighborhood. Economic forces that must be considered include such things as the existence of vacant or boarded-up properties in the neighborhood, and the level of essential local support services. Examples of governmental forces that should be taken into consideration include the regulations, laws, and taxes that are imposed on properties. Environmental forces that must be considered include, among other things, the existence of a hazardous waste site on or near the property, and the proximity of a property to an airport. Certain other factors that are not appraisal factors, such as the racial or ethnic composition of a neighborhood or the age or sex of the individuals who live in a particular neighborhood, must not be considered in the valuation process.

The appraiser must determine, analyze, and consider factors in the valuation process based on his or her identification of all forces or factors that have the potential to influence the value of the property. The appraiser must report neighborhood conditions in factual,

specific terms and be impartial and specific in describing favorable or unfavorable factors in a neighborhood. If an appraiser can demonstrate by market evidence that a characteristic has an effect on the value or marketability of the properties in the neighborhood, he or she must consider it in the valuation process. The appraiser must not make unsupported assumptions or interject personal opinion or perceptions about market forces or other factors that may or may not affect the use and value of a property. For example, a property located in an older neighborhood can be as sound an investment as a property located in a new neighborhood.

Degree of Development and Growth Rate

The degree of development of a neighborhood, which is referred to as "built-up" on the appraisal report forms, is the percentage of the available land in the neighborhood that has been improved. The degree of development of a neighborhood may indicate whether a particular property is residential in nature.

When reviewing an appraisal on a property located in a rural or relatively undeveloped area, the lender should focus on the characteristics of the property, zoning, and the present land use to determine whether the property should be considered residential in nature. For example, if the typical one-unit building site in a particular area (based on the zoning, the highest and best use of the land, and the present land use) is two acres in size, the mortgage will be eligible for purchase or securitization regardless of the percentage of the total appraised value of the property that the site represents, as long as the appraiser demonstrates through the use of comparable sales that the property is a typical residential property for that particular neighborhood.

Because Fannie Mae does not purchase or securitize mortgages secured by agricultural-type properties, undeveloped land, or land-development-type properties, the lender must review the appraisal report for properties that have sites larger than those typical for residential properties in the neighborhood. Special attention must be given to the appraiser's description of the neighborhood, zoning, the highest and best use determination, and the degree of comparability between the subject property and the comparable sales. If the subject property has a significantly larger site than the comparables used in the appraiser's analysis, the subject property may not be a typical residential property for the neighborhood.

Trend of Neighborhood Property Values, Demand/Supply, and Marketing Time

The appraiser must report the primary indicators of market condition for properties in the subject neighborhood as of the effective date of the appraisal by noting the information in the table below.

Trend of Property Values	Supply of Properties in the Subject Neighborhood	Marketing Time for Properties
<ul style="list-style-type: none"> • increasing, • stable, or • declining. 	<ul style="list-style-type: none"> • shortage, • in-balance, or • over-supply. 	<ul style="list-style-type: none"> • under three months, • three to six months, or • over six months.

The appraiser's analysis of a property must take into consideration all factors that affect value. Because Fannie Mae purchases mortgages in all markets, this is particularly important for neighborhoods that are experiencing significant fluctuations in property values including sub-markets for particular types of housing within the neighborhood. Therefore, lenders must confirm that the appraiser analyzes listings and contract sales as well as closed or settled sales, and uses the most recent and similar sales available as part of the sales comparison approach, with particular attention to sales or financing concessions in neighborhoods that are experiencing either declining property values, an over-supply of properties, or marketing times over six months. The appraiser must provide his or her conclusions for the reasons a neighborhood is experiencing declining property values, an over-supply of properties, or marketing times over six months.

When completing the One-Unit Housing Trends portion of the Neighborhood section of the appraisal report forms, the trends must be reflective of those properties deemed to be competitive to the property being appraised. If the neighborhood contains properties that are truly competitive (that is, market participants make no distinction between the properties), then all the properties within the neighborhood would be reflected in the One-Unit Housing Trends section. However, when a segmented or bifurcated market is present, the One-Unit Housing Trends portion must reflect those properties from the same segment of the market as the property being appraised. This ensures that the analysis being performed is based on competitive properties. For example, if the neighborhood contains a mix of property types not considered competitive by market participants, then a segmented or bifurcated market is present. Additionally, the conclusions reported in this portion of the appraisal will be supported by the analysis contained in the *Market Conditions Addendum to the Appraisal Report (Form 1004MC)*. The appraiser should also provide commentary on the other segment(s) of the neighborhood when segmentation is present.

Market Conditions Addendum to the Appraisal Report (Form 1004MC)

The lender must confirm that current market conditions are identified and analyzed in the valuation process and described in the appraisal report.

Form 1004MC is required for all mortgage loans delivered to Fannie Mae with appraisals of one- to four-unit properties. It is intended to provide the lender with a clear and accurate understanding of the market trends and conditions prevalent in the subject neighborhood. The conclusions regarding trends that are obtained from the 1004MC Form must be reported in the Neighborhood section of the report form.

In situations when there is not sufficient data to provide a meaningful analysis for the defined neighborhood, the form must be completed based on the information available, and an explanation must be provided. The lack of data may be an indication of the market conditions. If additional analysis of nearby areas that include competitive properties is performed, it must be discussed in the summary/conclusions section of the form. In any scenario, the Neighborhood section of the appraisal report must include the appraiser's conclusions regarding the housing trends.

For additional information concerning Form 1004MC, see [B4-1.2-01, Appraisal Report Forms and Exhibits](#).

Price Range and Predominant Price

The appraiser must indicate the price range and predominant price of properties in the subject neighborhood. The price range must reflect high and low prevailing prices for one-unit properties, two- to four-unit properties, condo units, or co-op units depending on the property type being appraised and the appraisal form being used. Isolated high and low extremes should be excluded from the range, which means that the predominant price will be that which is the most common or most frequently found in the neighborhood. The appraiser may state the predominant price as a single figure or as a range, if more appropriate.

Over-Improvements

An over-improvement is an improvement that is larger or costlier than what is typical for the neighborhood. For example, a 4,000 square foot home located in an area of homes where the typical home is 2,000 square feet may be considered an over-improvement. Furthermore, a home with an in ground pool in an area where pools are not typical may also be considered an over-improvement. The appraiser must comment on over-improvements and indicate their contributory value in the Sales Comparison Approach adjustment grid.

Improvements can represent an over-improvement for the neighborhood, but still be within the neighborhood price range, such as a property with an in-ground swimming pool, a large addition, or an oversized garage in a market that does not demand these kinds of improvements.

The fact that the property is an over-improvement does not necessarily make the property ineligible. However, lenders must review appraisals on properties with over-improvements that may not be acceptable to the typical purchaser to ensure that only the contributory value of the over-improvement is reflected in the appraisal analysis.

Age Range and Predominant Age

The appraiser must indicate the age range and predominant age of properties in the subject neighborhood. The age range should reflect the oldest and newest ages for one-unit properties, two- to four-unit properties, condo units, or co-op units depending on the property type and the appraisal form being used. However, isolated high and low extremes should be excluded from the range. The predominant age is the one that is the most common or most frequently found in the neighborhood. The appraiser may state the predominant age as a single figure or as a range when that is more appropriate.

When the age of the subject property is significantly different than the predominant age range, the appraiser must explain why the age is outside the range and comment on the marketability of the property and the adjustments that were made in the Sales Comparison Approach adjustment grid to reflect that condition.

Present Land Use

Fannie Mae's appraisal report forms provide an area for the appraiser to report the relative percentages of the developed land in the neighborhood when discussing the present land use, rather than simply referring to the zoning classifications. The appraiser must separately report the percentage of developed one-unit sites and two- to four-unit sites. Undeveloped land must be reported in the "Other" field. In addition, if there is a significant amount of undeveloped land in the neighborhood, the appraiser must include comments to confirm that he or she adequately described the neighborhood. If the present land use in the neighborhood is not one of those listed on the appraisal report form, such as parkland, the appraiser also must indicate the type of land use and its related percentage. The total of the types of land uses must equal 100%.

Typically, dwellings best maintain their value when they are situated in neighborhoods that consist of other similar dwellings. However, some factors that are typical of a mixed-use neighborhood, such as easy access to employment centers and a high level of community activity, can actually enhance the market value of the property through increased buyer demand. Neighborhoods may frequently reflect a blend of residential and nonresidential land uses.

When different land uses and property types are present in a neighborhood, that fact should be considered a neighborhood characteristic that the appraiser needs to take into consideration when performing the neighborhood analysis and defining the neighborhood boundaries. To confirm that any positive or negative effects of the mixed land uses are reflected in the sales comparison analysis, the appraiser should select comparable sales from within the same neighborhood whenever possible. If this is not possible, the appraiser may need to make neighborhood or location adjustments to the Sales Comparison Approach adjustment grid for any sales that are not subject to the same neighborhood characteristic.

Related Announcements

The table below provides references to the Announcements that have been issued that are related to this topic.

Announcements	Issue Date
Announcement SEL-2014-12	September 30, 2014
Announcement SEL-2014-03	April 15, 2014
Announcement 09-19	June 8, 2009
Announcement 08-30	November 14, 2008

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