My home appraised below purchase price. What now?

My property appraised too low

Whether you're buying, selling, or refinancing, a home appraisal that comes in too low could put the entire transaction in jeopardy.

So, what happens next? Ordering a second appraisal? Changing the sale price? Applying with a different lender? Something else?

Let's take a closer look at your best options after a low appraisal.

What a low appraisal means for you

An appraisal that comes in lower than the purchase price for your new home could derail your entire home buying process.

Mortgage lenders use the appraised value of the home to calculate your loan-to-value ratio (LTV), which is a big component in the underwriting process. LTV measures how much of a home's value the lender will finance.

Your LTV must stay within a loan's specific limits.

On an FHA loan, for example, your LTV can't exceed 96.5% of the home's appraised value. That means your maximum loan size for a $200,000 home would be $193,000. (The remaining $7,000 comes from your down payment.)

What happens if the appraisal is lower than the purchase price?

Lenders always use the appraised value to calculate your LTV — not the purchase price.

If the appraisal comes in lower than the purchase price, your lender will likely decrease the amount you can borrow. So, you'll either must pay more out of pocket or get the seller to lower their asking price.

As an example:

- Say you’ve agreed to pay $200,000 for a home
- You’re using an FHA loan; the maximum loan amount should be $193,000 (96.5% LTV)
- You plan to make a $7,000 down payment (3.5%)
- But the appraiser values your new home at only $190,000
- Your maximum mortgage size drops to $183,350 — 96.5% of $190,000
- With the reduced loan amount, **you’re now $9,650 short of the agreed-upon purchase price**

Unless the seller agrees to lower the price to match the appraisal, you will have to increase your down payment to get the same mortgage and interest rate.

Rather than paying $7,000 down you’d need to pay $16,650 down to buy the same $200,000 house.

Options for buyers with a low appraisal

When your home appraises for less than its purchase price, there are a few potential options:

- Seller and buyer renegotiate a new, lower home sale price
- Buyer increases the down payment to meet new LTV and down payment minimums
- Seller and buyer cancel the home purchase contract
- Buyer or seller requests an appraisal rebuttal (see below)

The possibility of a “bad appraisal” is why home purchase contracts are often written with an appraisal contingency.

Should the home fail to appraise for its contracted purchase price, the contingency clause allows buyers to re-evaluate and, potentially, walk away without losing earnest money.

In fact, FHA loans *require* this contingency in any purchases financed with FHA mortgages.

Appraisal contingencies are also sometimes used to renegotiate or exit contracts after an appraiser identifies required repairs, such as chipped paint or cracked windows.

As a home buyer, it's risky to waive your appraisal contingency. You may lose your negotiation leverage if the home appraises for less than its purchase price.

How to rebut or appeal your appraisal

The home buyer, in some cases, can request an appraisal rebuttal. This is a formal process in which the buyer's lender submits a request for the appraiser to re-examine the appraised price of the home.

Additional comparable homes may be submitted to the appraiser, as well as "missed" characteristics about the subject property that may add to its value.

However, these rebuttals often have little or no effect.

Appraisers are reluctant to change a home's value based on the report. The appraiser will submit a rebuttal response, stating that value has been changed based on new evidence, or that it wasn't changed and why.

Low appraised value for the home seller

If you're selling a home and it doesn't appraise for your listing price, a few things could be going on.

Your real estate agent may have listed the home too high. In this case, you may want to lower your asking price. It might be hard to find buyers who will kick in thousands of extra dollars to cover the difference, even in a seller's market.

And there's no guarantee that ordering another appraisal will yield the results you want.

In hot markets, though, it's common to list a home at a higher price, if competition will drive values up quickly. Some markets rise so fast that appraisal values can't keep up.

An appraiser must base your home's value on recent sales prices of similar houses.

Options for sellers with a low appraisal

Home sellers have a few options if the appraisal comes in low:

- Wait until a comparable home sell at a similar price
- Request that your buyer make up the difference in cash
- Lower your price to match the appraised value

The good news for sellers is that many buyers in today's market are flush with cash. So, it may not be as hard to find a buyer willing to cover the difference as it was in the past.

Some buyers may even agree to an 'appraisal gap guarantee,' which stipulates they're willing to pay extra cash in the event of a low appraisal.

What if your refinance appraisal comes in low?

Unless you're getting a **Streamline Refinance** through the FHA, VA, or USDA, you'll likely need a new appraisal to qualify for a refinance loan.

If the appraisal shows the current market value of your home is lower than expected, your new loan may not be large enough to accomplish all your goals.

Your options include:

- Appealing the appraisal
- Finding another lender who uses a different appraiser (you'll pay for the new appraisal)
- Doing a "cash-in" refinance, which involves bringing cash to closing to make up the difference between loan amount and the property value
- Taking out less cash than you'd planned (if you were doing a cash-out refinance)
- Cancelling the refi until you gain more equity

Keep in mind that cancelling the refinance won't cancel the appraisal fee you've already incurred. Likewise, ordering a new appraisal is no guarantee of a higher value, and you'll be on the hook for two appraisal bills.

Plus, the lender may not allow an additional appraisal.

Why does the appraised value affect your refinance?

Your appraisal affects your refinance loan because it helps measure the amount of equity in your home.

Home equity is your home's appraised value minus your mortgage debt.

For example, if you owe $150,000 on your current home loan and the appraisal process values your home at $225,000, you have $75,000 in equity.

If a different appraiser valued your home at $250,000, you'd have $100,000 in equity.

The amount of equity in your home influences interest rates and determines the size of your refinance loan. It also determines what 'extra' benefits you can get from a refinance.

For instance, if you have at least 20% equity and your current mortgage is an FHA loan, you could likely refinance into a conventional loan to **remove your mortgage insurance payments**.

If you want **cash-out** when you refinance, you'll need significantly *more* than 20% home equity. That's because lenders require you to leave at least 20% equity untouched when you cash out.

Human versus automated appraisals

Many refinance lenders today are going with automated appraisals (AVMs) to save time and money.

If you have made many home improvements since your purchase, or your home interior has features not obvious to a "drive-by" appraiser, you may want to insist on a human appraiser, even if it costs more.

One point to bring up: It's very common for homeowners to overestimate the value of their own homes. So, it's best not to get your heart set on a certain home value or cash-out amount until you've had an official appraisal to check the home's current value.

Low appraisal value for new construction

Home appraisals for renovation loans or new construction loans work a little differently. The appraiser will need to measure the market value of a home that doesn't yet exist.

To do this, the appraiser will study your building plans along with your local housing market to determine the home's eventual value.

Many lenders call this a "subject-to" appraisal since it is subject to your planned project's completion.

Once the builder finishes the job and the home receives its Certificate of Occupancy, you'll need a new loan to pay off the construction loan's balance. This new loan is called "permanent" or "take-out" financing.

If, for some reason, your newly built house did not appraise for a loan large enough to pay off construction costs, you'd have some of the same options as any homebuyer:

- Try a new lender
- Get a new appraisal
- Ask the builder to take less money

If the low appraisal is the builder's fault — say, the quality of construction or materials were not as described in the loan application documents — you may be able to sue your builder to recoup some of the losses.

A lot of **builder-owners** get construction-to-permanent (C2P) loans which combine the construction loan and the permanent mortgage into one loan. This option has both advantages and disadvantages. One advantage: You'd likely need only one appraisal instead of two.

New construction that is not custom

If your newly built house is in a planned development, and you are financing it with a traditional mortgage, you're in the same boat as any other buyer of a pre-built house.

You have the same options if an appraisal comes in low — back out, renegotiate, make a bigger down payment, etc.

Low appraisals and FHA 203(k) loans

If you finance your home construction with an **FHA 203(k) rehab home loan**, you might get lucky. The agency allows 10% "wiggle room" on the final appraised value without it affecting your loan terms.

This also applies if you use a 203(k) refinance to add some home improvements when you refinance your property.

How appraisers determine your home value

Apart from no-appraisal, Streamlined Refinance loans, nearly every mortgage application requires a home appraisal.

While many lenders use automated valuation models (AVMs) to get an idea of your property value, most transactions still involve a licensed human.

Licensed home appraisers use three common methods to determine your property value:

The 'sales comparison' approach

For home buyers and homeowners financing primary homes, the "sales comparison" method is the most common.

Using this method, a home appraiser compares the subject property (i.e. your home) to other, similar homes in the immediate vicinity.

"Immediate vicinity" varies by region:

- In a dense city such as Seattle, Chicago, or San Francisco, the immediate vicinity for a home will be within 0.25 miles — usually not more than a few city blocks
- In less-dense areas, the immediate vicinity of the subject property could range to several miles

Appraisers are most interested in sales of similar homes within these areas. They look at such traits as:

- Number of bedrooms
- Number of bathrooms
- Age of home
- Quality of home finishes
- Square footage

They also consider the "appeal" of a home based on things like school districts and proximity to traffic and shopping.

Then, for each comparable home, appraisers search public records for home descriptions, sales data, and other available information about a property. This data is used to formulate the value of the subject property.

Suppose the nearly identical home across the street recently sold for $600,000. However, it does not contain a finished basement like yours does. So, your house might appraise for $620,000.

Comparable homes sold in the most recent 90 days are hugely important in the sales comparison approach. Homes sold over six months ago are less relevant.

Other home appraisal approaches

There are two other methods for appraisers to value property — the replacement cost approach and the income approach.

The replacement cost approach estimates what it would cost to buy your lot and build a house like yours, then subtracts depreciation.

This method is useful if you're shopping for home insurance and want all potential insurers to have the same home value information. However, insurers will come up with their own valuation when they underwrite your policy.

For the income approach, an appraiser researches rental data in your housing market to determine what your home would rent for on the open market and uses this information to calculate your property value.

The income valuation approach is most used for investors and landlords.

3 more ways to determine your property value

In addition to the home appraisal, there are three more ways to determine a home's value. They are, from least to most accurate:

1. **Automated Valuation Model (AVM)** — A computer program assesses your home's value based on available market data

2. **Comparative Market Analysis (CMA)** — Your Realtor analyzes the local real estate market to help you decide on an offer price or listing price
3. **Broker Price Opinion (BPO)** — A mortgage broker assigns the value of the home

The method you choose depends on your goals. Each valuation tool has its merits and drawbacks. Let's take a closer look at each one:

Automated valuation model (AVM)

You can find automated valuation models, or AVMs, online for free. These models estimate your property value by analyzing local listings and public record data, determining trends, and applying them to your property.

If recently sold, similar-sized homes ("comps") in your area are changing hands for 10% more than they did when you purchased your property, your estimated value will probably be about 10% more than your purchase price.

This is a basic evaluation.

For instance, the software has no way of knowing if you just gutted your kitchen and added $50,000 in equity.

An AVM also doesn't always "know" if some of the comps were distress sales, artificially lowering their prices, or if defects in a comp's title affected its value. Likewise, it doesn't know if a bidding war increased an area's sale price above typical market values.

AVMs are useful for demonstrating trends — the direction and extent of changes in area values — but they're much less helpful for valuing specific property.

Comparative market analysis (CMA)

You can usually get a free home value estimate from a real estate broker or agent. They do them all the time for potential home sellers.

This client sales presentation (for that's what it is) is called a CMA, or comparative market analysis.

The CMA is only as accurate as the agent's knowledge of the area. Realtors typically "eyeball" property differences and make judgments based on their experience.

A CMA can provide useful data when you're coming up with an asking price. However, you should understand an agent's main business is not evaluating. It's possible an agent could overstate your appraised value to get your listing.

Broker price opinion (BPO)

Paying a broker price opinion (BPO) could yield a more accurate valuation.

Brokers with BPOR certification from the National Association of Realtors have completed special training to do this work, and lenders often commission BPOs to determine the value of foreclosure homes before putting them up for sale.

To perform a BPO, the broker examines three recent local sales of property similar to yours and three currently listed houses. The broker compares the condition and features of these homes to yours, makes numeric adjustments according to formulas, and offers a value estimate.

A BPO costs between $50 and $125 for a typical home.

Can you get a redo on your appraisal?

Homes don't often appraise for less than their purchase price — especially in a rising home value environment. However, it can happen, so it's best to know your options.

In some cases, you may want to try a different lender to get a second opinion on the home's value — especially if you have data showing the first appraisal was inaccurate.