

Bidding Wars, Cash Offers, Record High Prices: What you need to know about appraisal contingencies in today's housing market

The upsides of a seller's market can have downsides for loan officers and real estate agents, including a relatively nascent phenomenon known as the appraisal gap.

It continues to be a remarkable time for professionals who support the residential real estate industry. Many are comparing it to The Great Gold Rush. Like the flood of prospectors seeking fortune in 1849, today's potential home buyers far outnumber available properties.

To sweeten their bids, many potential buyers are offering well above asking price and waiving traditional contingencies such as the bank appraisal. While these strategies can help a buyer secure their dream home, they also can create bumps in the road to closing when the appraisal value comes back less than the buyer's purchase price. This results in an appraisal gap that can derail your sale.

When the appraisal gap is smaller – say \$10,000 to \$15,000 less than the offered price -- the gap may be

resolved by negotiating a lower price with the seller, bringing more cash to the closing, or a combination of both. But when the appraisal gap is wide, making up the difference with a greater cash down payment can be much more difficult -- if not impossible.

“At today's skyrocketing home prices, the majority of buyers simply don't have the additional cash on hand needed to cover an unexpected appraisal gap,” says Dave McCormick, Senior Vice President with Radian. “This can create havoc for all involved as buyers scramble to come up with additional cash and sellers often put pressure on their listing agents to go with a higher backup offer.”

Where does the additional cash come from? Tapping into investment or retirement accounts may be an option, but many potential buyers would rather not liquidate long-term assets or otherwise make early withdrawals. A gift from family is another solution, but that is not always available. So what's left?

We're all familiar with mortgage insurance as the go-to solution for buyers who start their home search with less than 20% down,” notes McCormick. “It's a simple and nearly seamless solution that can also work for buyers facing an appraisal gap.

Whether you are the buyer or seller, real estate agent or lender, McCormick says a simple and straightforward way to save your deal may be through traditional mortgage insurance.

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In certain instances mortgage insurance can be used to shift the loan-to-value ratio (LTV) and restructure the loan so that it includes some or all of the appraisal gap. This significantly reduces or eliminates the amount of additional cash required for closing.

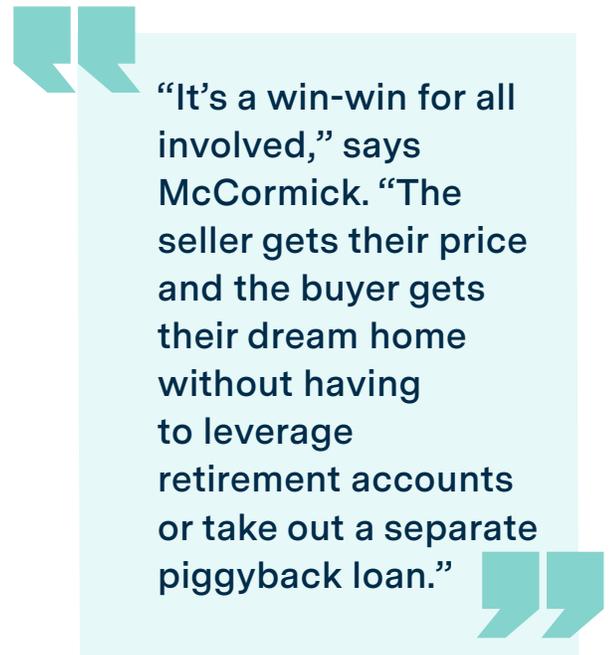
“In most cases, it's going to be a lot easier for a buyer to come up with a few thousand dollars to cover mortgage insurance than it would be to come up with \$30,000 or more to close the appraisal gap,” McCormick says.

Risk-based pricing makes mortgage insurance particularly cost effective for high FICO buyers. And with a single lender paid premium, the cost of the mortgage insurance may be included in the loan so that there is no additional associated expense at closing.

“It's a win-win for all involved,” says McCormick. “The seller gets their price and the buyer gets their dream home without having to leverage retirement accounts or take out a separate piggyback loan.”

Given the wild roller coaster ride of price escalation in today's market, it can be helpful to discuss appraisal gaps and possible mortgage insurance solutions with potential buyers before they make an offer. Doing so can give them a better understanding of their buying power, not to mention minimize any panic that may result if/when they receive a bank appraisal that is significantly less than their offered price. In addition to exploring the mortgage insurance option, buyers may want to consider adding an [appraisal contingency to their sales contract](#).

Are you in an appraisal gap market? Resolving appraisal gaps with mortgage insurance may be a fast and easy way to keep your deal on the table. Please reach out to a Radian representative to learn more.



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