MODERNIZING APPRAISALS: A REGULATORY REVIEW AND THE FUTURE OF THE INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND INSURANCE

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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MODERNIZING APPRAISALS: A REGULATORY REVIEW AND THE FUTURE OF THE INDUSTRY

Wednesday, November 16, 2016

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING
AND INSURANCE,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2128, Rayburn House Office Building, Hon. Blaine Luetkemeyer [chairman of the subcommittee] presiding.

Members present: Representatives Luetkemeyer, Pearce, Posey, Ross, Barr, Rothfus, Williams; Cleaver, Velazquez, Clay, Green, and Beatty.

Ex officio present: Representative Waters.

Also present: Representative Sherman.

Chairman LUETKEMEYER. The Subcommittee on Housing and Insurance will come to order. Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "Modernizing Appraisals: A Regulatory Review and the Future of the Industry."

Before we begin, I would like to thank the witnesses for appearing before the subcommittee today. We look forward to your testimony. I now recognize myself for 5 minutes to give an opening statement.

Many homeowners don't focus on appraisals until something goes wrong, or until they can't get one. It is not an area in which Congress spends much time debating or one that the media covers intently, but appraisals are one of the cornerstones of the home-buying process. Issues that impact appraisers also impact nearly every American buying or selling a home in rural and urban areas, in high- and low-income neighborhoods.

These issues affect lenders, home builders, real estate professionals, and ultimately, the health of the American economy, and the manner in which appraisals are regulated merits the attention of this subcommittee. The appraisal profession has changed dramatically since the last major regulatory overhaul with passage of FIRREA in 1989. The finance mortgage system has changed, and alternative valuation methods are more advanced than ever. Yet when it comes to the regulatory regimes surrounding appraisals, it seems we are stuck in 1989. Let's do a quick overview of the system in place today, as I understand it.

The Appraisal Subcommittee, a body comprised of seven Federal regulators, regulates the standards and requirements of each State appraisal board. The Appraisal Foundation, a nongovernmental entity chartered by Congress, promulgates those standards and requirements for the States, but lacks any meaningful regulatory authority. That authority lies in the States, which go through the actual process of credentialing the appraisers based on the criteria set by the Foundation. We have licensed appraisers, certified appraisers, and general—certified general appraisers. We have appraisal management companies that act as a third party in selecting appraisers. This is not a simple regime, and it impacts homeowners.

Perhaps as a result of some of this regulatory bureaucracy, the appraisal industry is experiencing a shortage that is beginning to harm the housing market. We are seeing delayed closings and increased consumer costs. This shortage is hitting rural areas particularly hard, including rural Missouri, which I am very familiar with.

Today's hearing will give us an opportunity to investigate the past, present, and most importantly, the future of appraisal regulation. I personally would like to see a more State-centric model of regulation, one that cuts some of the Federal bureaucracy hovering above appraisers today.

Beyond the regulation of appraisers, we should look at the current regime—what the current regime requires of lenders, builders, and home buyers. We need to examine alternative home valuation methods that employ the most modern technologies and foster greater consumer choice. We should look at the individuals who should and should not be qualified to do an appraisal and deploy resources accordingly.

In rural Missouri, for example, where today there may be one appraiser for every two counties, there needs to be an alternative. We need to address this in the changing marketplace. Dodd-Frank attempted to address some of the shortcomings seen in the appraisal market, but the law's impact has not enhanced the system for appraisers, stakeholders, or most importantly, consumers. Appraisal is important. They instill confidence and guard against housing markets that could otherwise become depressed.

We live in the 21st century, and the market deserves 21st-century solutions. It is long past time to examine this model regulation and find a better way. Again, I want to thank the witnesses for appearing before the committee today. I look forward to an open conversation.

And the Chair now recognizes the ranking member of the subcommittee, the gentleman from Missouri, Mr. Cleaver, for 5 minutes for an opening statement.

Mr. CLEAVER. Thank you, Mr. Chairman. We are holding this hearing on the role of—that appraisals play in the housing market, and this will give us the opportunity to discuss changes that have been made to the appraisal system following the Dodd-Frank Act that went into effect in 2010. As we all know, the States are responsible for much of the regulations for the appraisal process, including the certification and licensing of appraisals, as well as the registration of appraisal management companies.

The Federal Government also plays a role in a more general oversight working to create more uniform standards, and the Financial Institution Recovery Reform and Enforcement Act of 1989 originally sought to oversee appraisal standards, but many of those provisions were updated with the passage of the Dodd-Frank Act, including independent appraisal requirements and the duty to report on appraisers who violate the law, and during the housing crisis, they were many.

It has been a hard 6 years since the start of the housing crisis, though this committee has spent a considerable length of time working to staunch the bleeding, and many of the wounds are still healing. The fraudulent inflation of home prices by some dishonest appraisers did, in fact, play a significant role in the housing crash, and it is imperative that we continue to impose high standards to ensure the safety and soundness of the housing market but also, to protect the honest, hardworking appraisers.

During the debate over Dodd-Frank, I can remember those seats being taken by individuals who gave us horror stories about what appraisers—some appraisers were doing. But I do think that—I mean, at least I try to be careful that we don't somehow demean all appraisers. But I believe it is necessary to uphold appraisal independence to ensure that lenders operate independently from appraisers without unduly putting pressure to overinflate prices.

I also have a number of questions regarding the alternative valuation methods where computer systems are used to determine the value of mortgages. While Dodd-Frank bears sole reliance on these systems, I do, in fact, have concerns that a move toward higher use of computerized modeling would be detrimental to the housing market, so I appreciate you being here today, and I look forward to becoming dialogical as the committee hearing goes on. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. I thank the gentleman. I now recognize the gentleman from Texas, Mr. Green for the balance of the time.

Mr. GREEN. Thank you, Mr. Chairman, and I thank the ranking member as well. I do believe that we have some room for improvement in this area, and I think that some of the things that I have heard from people who have had actual experiences are—would merit some consideration. I talk to realtors, I talk to the lenders, and I have talked to the people who actually do some of this appraising, and there appears to be space for improvement.

It seems that one of the overriding concerns is a lack of an appeal process, a lack of a process that allows for a dispute to be resolved when it comes to the value of property. And another area of concern appears to be how long will an appraisal stay with the property before you can have another appraisal, assuming that you have applied for an FHA loan. Conventional loans are a little bit different from the FHA loans.

These FHA loans are desired for various and sundry reasons. The hard stop on a FHA loan may not be the same as conventional, so people want the better product. But in getting the better product, they are having some concerns that I think we should look at. But I also think that as we look at these concerns, we should make sure that we don't just completely do away with some things that have been that are beneficial. This is the old baby-in-bathwater argument. I think that there are some things that are beneficial that we have to maintain and should maintain, but I do believe that in a major piece of legislation, there are opportunities to make corrections that are sometimes called "technical corrections," and I would support what the ranking member has said in terms of our desiring to be amenable to looking at some of these things, and I yield back the balance of my time.

Chairman LUETKEMEYER. The gentleman yields back. Today we welcome the testimony of Mr. James Park, executive director of the Appraisal Subcommittee; Mr. David Bunton, president of the Appraisal Foundation; Ms. Joan Trice, chief executive officer and founder of Clearbox; Mr. Bill Garber, director of government and external relations from the Appraisal Institute; Mr. Ed Brady, chairman of the board, National Association of Home Builders; and Ms. Jennifer Wagner, managing attorney, Mountain State Justice, Incorporated.

You will each be recognized for 5 minutes to give an oral presentation of your testimony. And without objection, your written statement will be made a part of the record. And just to give you a little primer on the lights in front of you, green means go, yellow means you have 1 minute to wrap up with your testimony and all the questions that you see around us when we ask you, and red means time to stop. I do have the last say.

So with that, Mr. Park, you are recognized for 5 minutes. Welcome.

STATEMENT OF JAMES R. PARK, EXECUTIVE DIRECTOR, APPRAISAL SUBCOMMITTEE

Mr. PARK. Good morning, Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee, thank you for the opportunity to testify before you this morning. My written testimony details the history of appraisal regulation, the Appraisal Subcommittee, our current operations, and the added responsibility and authority given to the ASC through the Dodd-Frank Act.

Given my limited time before you this morning, I will focus my comments on the discussion topics as requested by this subcommittee.

First, regarding alternative valuation methods. This is nothing new. The GSEs, lenders, and others have been using them for many years. While technological and innovation is needed and should be encouraged, care should be taken to develop valuation techniques that do not rely solely on technology and big data, but also rely on the professional expertise provided by an appraiser.

Unlike appraisals, there are no generally accepted standards for development or use of AVMs, or automated valuation models, evaluations, or hybrids. Automated tools are easily manipulated, and overreliance could lead to misleading conclusions, fraud, and abuse. Automated tools also have limited use in rural and urban areas where data is scarce or unreliable.

Second, regarding the appraiser shortage. It appears that economic conditions in certain parts of the country have increased demand for appraisal services. What is not clear is the cause of these localized supply-and-demand issues, and the veracity of news reports on the topic is questionable. Part of the problem may be that many appraisers refuse to accept mortgage lending assignments due to low pay, confusing or burdensome conditions, fear of blacklisting, and a perception that lenders don't value their opinions.

However, I am concerned about the lack of new entrants into the profession compared to the numbers of appraisers leaving. This has been a trend for several years now and could lead to problems in the future.

In 2008, Congress passed a Housing and Economic Recovery Act, HERA, requiring FHA to only accept appraisals performed by certified appraisers and barring the use of licensed appraisers. Since HERA, many lenders have followed suit, effectively removing otherwise qualified appraisers from mortgage lending. This is a particular problem in rural markets.

Third, regarding the de minimis value threshold. The Federal financial institutions regulatory agencies set the de minimis threshold with CFPB concurrence. Questions regarding the threshold should be directed to those agencies.

Fourth, regarding the streamlined Federal regulatory regime, the ASC recognizes the importance of a streamlined regulatory system and has taken several steps to promote one. Details are in our written testimony.

Related to other areas that could be streamlined or improved, standardize the varying requirements placed on appraisers by the GSEs, FHA, VA, Federal regulators, and lenders. Today's current cornucopia of statutes, rules, and guidelines, some of which continually change, are confusing and burdensome to all.

Require the GSEs to share with appraisers data being collected from appraisal reports through the GSE's collateral portals. Modernized use of appraisals in mortgage lending allow appraisers to provide a reasonable range of values. Low-risk transactions are sometimes denied or canceled when the appraised value is just slightly below the value needed to make the deal work.

Lastly, regarding replacing the current system with a State-based regulatory structure. Currently, we have an effective system that draws on the strengths of the States, private sector, and Federal Government. The system also largely relies on appraisers to regulate other appraisers. Replacing the Federal regulatory structure with a State-based regulatory system would greatly complicate, not streamline, the system. Cost to consumers and lenders would increase and unnecessarily burden the mortgage finance system as States would almost certainly implement varying laws and regulations. There are already examples of this in the States.

In conclusion, throughout my career in the private sector and now in the Federal Government, I have dealt with a complicated array of Federal and State laws, regulations, and guidelines, and I can assure you that the industry seeks more standardization, not less. While the current system respects and supports States' rights, I want to impress upon you the importance of a national minimum baseline of enforceable appraisal standards and appraiser qualifications to facilitate Congress.

Turning appraisal regulation back to the States would likely be counterproductive as it would increase regulatory burden and cost and likely further restrict consumer access to purchasing a home and credit, in general.

Thank you for the opportunity to appear before the subcommittee, and I look forward to answering any questions.

[The prepared statement of Mr. Park can be found on page 96 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Park.

Mr. Bunton, you are recognized for 5 minutes.

STATEMENT OF DAVID S. BUNTON, PRESIDENT, THE APPRAISAL FOUNDATION

Mr. BUNTON. Thank you, Mr. Chairman, Ranking Member Cleaver, and members of the subcommittee. The Appraisal Foundation greatly appreciates the opportunity to appear before you today and to offer our perspective on the regulation of real estate appraisers.

By way of background, I've served as a senior staff member of the Foundation for the past 26 years and have the privilege of serving on the Congressional staff for a dozen years prior that.

Let me just begin with a few words about who we are and what makes us different. One, we are a not-for-profit organization that was founded before the enactment of FIRREA. We are not an advocacy group or a trade association, but rather an umbrella group that represents about 100 organizations, and they range from the American Bankers Association to the Department of Veterans Affairs, from the National Association of Home Builders to the Department of Interior.

Essentially an appraiser regulatory system, we are the private sector expertise. We do not have a—as the chairman pointed out, we don't have any regulatory authority, but we provide the tools to the regulatory community. For example, we set the minimal qualifications that you need to get a State credential education experience. We write the exam that is used by all 50 States in five territories, and we also are the authors of the generally recognized standards of conduct, the Uniform Standards of Professional Appraisal Practice that all State-licensed and certified appraisers must adhere to. We have also been a resource to numerous Federal Government agencies, and currently have cooperative agreements with the U.S. Department of Energy and the Department of Justice.

To address the points that were referenced in your invitation to testify, I would like to offer the following:

We do have a very unique Federal, State, and private sector partnership that has grown and matured over the past quarter century. It is effective and operates solely on user fees paid by appraisers. There are no government-appropriated funds involved in this, and we believe this could be a model for other regulatory programs.

Regarding the effectiveness of the Appraisal Subcommittee, the implementation of a rating system of the State appraiser regulatory programs and the appointment of policy level representatives to the subcommittee have been very positive steps in recent years. However, we believe there are few opportunities for improvement in its current structure.

Dodd-Frank and its impact on the current regulatory system, stakeholders, and consumers. The focus on appraiser independence, the regulation of appraisal management companies, and the elimination of some predatory lending practices were all positive outcomes. However, there have been several unintended consequences of those decisions, which we look forward to discussing with you today.

The de minimis threshold in Federally related transactions. According to the National Association of Realtors, the average sale price of an existing home is $230,200. The current level of the de minimis is $250,000. You can make the argument it is already too high, and we are certainly in opposition to any increase to the $500,000 level.

We also believe that efforts should be made to restore the definition of what constitutes a Federally related transaction, back to what Congress originally intended when FIRREA was enacted in 1989.

A shortage of appraisers. There is no question that there is currently a shortage of appraisers in certain markets. It is not a national shortage, but in certain markets, particularly in rural areas and areas that have seen an uptick in mortgage originations, there is a shortage. We have—there are several reasons for this, no one reason, and I look forward to sharing those reasons with you this morning.

Appraising in the 21st century. As long as we have a collateral-based lending structure, there will always be a need to determine the underlying value of the security for a loan. While we may have entered the age of big data, the analysis of that data by a trained valuation professional has never been more important. An example for that would be what happened 9 days ago. The day before the election, we all were exposed to a great deal of very precise data, and we all learned 24 hours later, it was not accurate data. So that is an example of where—you can trust the numbers but you need some human intervention there.

In conclusion, today we may hear testimony that will contain proposals that range from creation of a new large Federal bureaucracy to one that all but eliminates Federal oversight. The current Title XI real property appraiser regulatory system, while unique and not without its flaws, it has made a real positive difference over the past quarter century. It promotes consistency among the States due to the appropriate Federal oversight. It has instilled competency by ensuring that we have meaningful standards and qualifications, and a uniform national exam, none of which existed before the enactment of FIRREA, and it operates at no cost to the taxpayers, and there are no Federally appropriated funds.

Appraisers have historically made a significant contribution to the safety and soundness of our financial system, and their important role will continue in the future. The catalyst for the creation of this current appraiser regulatory system was to protect the integrity of the deposit insurance fund, a need that is as strong today as it ever was. The Foundation stands ready to assist with any effort to make the current system more efficient.

Again, we appreciate the opportunity to share our perspective with you, and we urge this subcommittee and all Members of Congress to continue to use the Foundation as a fair, impartial, and objective resource. Thank you very much.

[The prepared statement of Mr. Bunton can be found on page 51 of the appendix.]

Chairman LUETKEMEYER. Mr. Bunton, you are very, very good. That was exactly 5 minutes. That is amazing. Thank you very much for your testimony.

Ms. Trice, you are recognized for 5 minutes.

STATEMENT OF JOAN N. TRICE, CHIEF EXECUTIVE OFFICER AND FOUNDER, CLEARBOX

Ms. TRICE. Chairman Luetkemeyer, Ranking Member Cleaver, and members of the Subcommittee on Housing and Insurance, thank you for the opportunity to share my thoughts regarding, "Modernizing Appraisals: A Regulatory Review and the Future of the Industry."

My name is Joan Trice, and I am speaking on behalf of no one in particular, but anyone who desires to uphold appraisal independence. Today, all stakeholders suffer from appraisal regulatory regime that is outmoded. The housing finance crisis shed a bright light on the systemic failures of the appraisal process.

The structural flaws of the regulatory schema reveal a system whereby no one was held accountable. This illustration of the current regulatory system says it all. It should be no surprise that giventhe above diagram, that the appraisal industry is being highly scrutinized. It is entirely dysfunctional. It is time for big and bold, a plan to overhaul the system.

The appraisal profession needs a single authority to take ownership of the policy, process, practice, procedures, and the people who are licensed. National licensing is needed with oversight at the State level. States must adopt a standardized process for investigation and adjudication of any disciplinary actions. Peer review and rehabilitation of the appraiser should occur at the State level.

This new entity should not carry forward any of the legacy agencies that exist today. The times call for a fresh holistic solution to replace the disjointed ineffective structure that currently exists. Repeal FIRREA Title XI and replace it with this new independent agency.

Independence is the cornerstone of the appraisal process. The home valuation code of conduct, and subsequently the appraisal independence requirement components of Dodd-Frank, left an indelible mark on the appraisal profession. For the last 9 years, practically every single stakeholder has done their best to avoid compliance with the appraisal independence requirements. Appraisal is truly the weak link, and our current policies and systems continue to diminish the important role that appraisers play in the housing finance ecosystem. Discussions of shortages, poor quality, cost, delayed delivery of appraisals, and the de minimis threshold are all code for efforts to diminish the role of the appraisal process.

The events of the presidential election offer a cautionary tale. Big data failed, models failed, bias and lack of independence by the analysts failed. Fannie Mae and Freddie Mac would have you believe that they hold all the marbles. Once again, they are competing with each other by reducing appraisal requirements. This is a race to the bottom, and we have seen this movie before, and we know how it ends.

Do not think for a minute you can replace appraisers with push-button technology. Appraising is part art and part science. Create a system whereby well-trained ethical appraisers have access to reliable data and afford them the independence to play their important role.

In conclusion, if Congress is truly serious about the safety and soundness of the housing finance system, then there is only one clear path for the appraisal process to thrive. Establish a single authority over real estate appraisal. The white paper entitled, "Reengineering the Appraisal Process" I provided explores in greater detail solutions to bolster the appraisal profession.

Thank you for the opportunity to share my thoughts on this important topic.

[The prepared statement of Ms. Trice can be found on page 116 of the appendix.]

Chairman LUETKEMEYER. Thank you, Ms. Trice.

Mr. Garber, you are recognized for 5 minutes.

STATEMENT OF BILL GARBER, DIRECTOR OF GOVERNMENT AND EXTERNAL RELATIONS, APPRAISAL INSTITUTE

Mr. GARBER. Mr. Chairman and members of the subcommittee, on behalf of the largest professional association of real estate appraisers in the United States, thank you for holding this hearing. Real estate appraisal plays a critical role in the American economy by helping financial institutions conduct risk management and make safe and sound loans.

Today, the number of appraisers in the United States is on the decline, and banks and real estate professionals are expressing concerns about a potential shortage of appraisers. Appraisers routinely are being buried by rules and regulations in nearly every facet of their business, from how an appraiser reports an appraisal through supervising trainees, uneven licensing requirements to licensing and registration fees passed down by clients, to mandates from Federal agencies, appraisers' professional lives have become overly complicated, more expensive, and less productive due to a dated and archaic regulatory structure that needs to be revised and updated to the reflect today's market.

Real estate appraisers face a layering effect of rules and regulations that create a disincentive for potential entry into the profession, while also diminishing the profession's profitability. This is counterproductive, given that rules and regulations continue to grow in number every year. These include background checks with no Federal mandate or efficient processing system, unappealing supervisory appraiser and trainee appraiser requirements, and constantly changing rules and standards.

While we appreciate the role and function of the various organizations and agencies that have been part of the appraisal regulatory structure since its beginnings in 1989, the appraiser regulatory structure today is overly complicated. The primary functions of the Appraisal Subcommittee can and should be performed more efficiently, and without perpetually taxing appraiser practitioners and users of appraisal services.

And the Appraisal Foundation's role in setting standards and qualifications, a role that is carried out reasonably well, should be unimpeded by unrelated activities. In short, the continuous state of change forced on the profession can be simplified and made more accountable. As such, the Appraisal Institute believes there is a better, less complicated approach that would improve appraisal quality, reduce costs, and address fundamental concerns that are driving away appraisers from the profession.

We believe that our proposed model would benefit from the combined experiences of other industries and precedents established by Congress. Specifically, we suggest that Congress modernize the appraisal regulatory structure and align it with those in the real estate and mortgage industry using a model like the Nationwide Mortgage Licensing System cooperative among State agencies.

Authorizing the appraisal profession to utilize a system like the NMLS for its certification and licensing system would enable State appraiser regulatory agencies to benefit from enhanced communication with other State agencies, including those outside of appraisal such as State banking regulatory agencies. Such a realignment would also provide a common system for appraisers to submit applications for licensure in multiple States.

Today, appraisers who wish to earn and carry licenses in multiple states must separately apply in each State, significantly adding to administrative requirements and obligations. The most direct example of the benefits of such a system involves background check requirements that currently are being imposed on appraisers on a State-by-State basis. Several years ago, the Appraisal Foundation established a fingerprint-based background check requirement for States.

Today, 47 States now have in place a requirement for formal background checks. Many States impose similar requirements on existing credentialed holders in real estate appraisal, many of whom have been practicing in good standing without any issues for many years. A few States even went so far as to impose these requirements on appraisers practicing in other States who applied for a license via reciprocity or a temporary practice permit.

Even though the Appraisal Foundation had the best intentions, it eventually backed away from this requirement, acknowledging that it had erred. Now it is unlikely that States will repeal or change the existing requirements anytime soon. Under an NMLS-like system, such background checks could be performed and shared by all participating State agencies hoping to significantly shave its burdensome administrative expense.

In conclusion, the Appraisal Institute is not suggesting eliminating all Federal involvement in the appraisal regulatory structure, but rather repositioning it to align with regulatory systems of other related industries. Should States fail in their responsibilities to manage appraisal oversight, a specified Federal agency like the FDIC, or FHFA could be authorized to set up a backstop system just as the statute recognizing the NMLS does today. Such a system simply would reposition the Federal role to one of a backstop authority of one of last resort.

Presently, real estate appraisers pay for the operation and maintenance of the regulatory structure through license renewal fees, course requirements, and mandates to purchase the volume of rules and regulations. After almost 27 years of FIRREA, it is time to make the appraisal regulatory structure and process more efficient and reposition—and responsive to the needs of practitioners and consumers.

The Appraisal Institute applauds Congress' review of the FIRREA statute with an eye towards modernizing the appraisal regulatory structure, and we stand ready to assist you in any way we can. Thank you for giving us the opportunity to testify today, and I would be happy to answer any questions.

[The prepared statement of Mr. Garber can be found on page 76 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Garber.

Mr. Brady, you are recognized for 5 minutes.

STATEMENT OF ED BRADY, CHAIRMAN OF THE BOARD, NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. BRADY. Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee, I am pleased to appear before you today on behalf of the National Association of Home Builders to share our views on the regulatory structure of the appraisal industry and suggestions for ensuring efficient and effective collateral valuation.

My name is Ed Brady, and I am a home builder and developer in Bloomington, Illinois, and sitting here as NAHB's 2016 chairman of the board.

The housing recovery has been impeded by ongoing problems in the U.S. residential appraisal system. While lenders, Federal banking regulators, and Federally related housing agencies implemented corrective measures in response to valuation breakdowns in the wake of the Great Recession, And Congress mandated additional measures in the Dodd-Frank Act, these steps did not address fundamental flaws and shortcomings of the residential appraisal framework.

Improper appraisal practices, a shortage of experienced appraisers, and inadequate oversight of the appraisal system continue to restrict the flow of mortgage credit and retard the housing recovery. NAHB is not advocating that appraisals should be higher than the market. Rather, our goal is to establish an appraisal system that produces accurate values through all phases of the housing cycle.

The focus of reforms, to date, have been on eliminating undue influence on appraisers to produce inflated valuations. However, when home prices began declining, improper appraisal practices exasperated the sliding values. Some appraisers used distress sales, many of which involve properties that were neglected and in poor physical condition as comparables in assessing the value of a brand new home, without accounting for major differences in condition and quality. Without such adjustments, the two housing types are just not compatible or comparable.

As the housing market has improved, builders face new appraisal challenges, specifically the lack of data on new construction, a shortage of appraisers experienced in appraising new construction, and no practical way to appeal a faulty appraisal. Getting more new home transactions into multiple listing services' databases would be a simple solution for the lack of data. NAHB is presently engaged in that discussion, and this, we hope, to result—have results soon.

Through dramatic increase in the use of appraisal management companies, or AMCs, has led to more activity by appraisers with less training and experience. This is problematic for new home construction transactions, which by their nature, are very complex.

Appraisers must be able to analyze detailed plans and specifications, determine the value of options, including state-of-the-art energy efficiencies, find appropriate comparables, and factor in land values. One way to improve the quality of new home valuations is to strengthen education, training, and experience requirements for appraisers of new home construction.

The biggest flaw in the current appraisal system is the lack of workable appeals processes. Current valuation practices do not provide a process for expedited appeals of inaccurate or faulty appraisals. Buyers and sellers, builders and real estate agents can be held hostage by the current inability to promptly address legitimate questions on evaluation. NAHB recommends the adoption of a standard appraisal appeal structure similar in design to the one utilized by the VA.

Finally, the current residential appraisal system continues to face many challenges due to inconsistent and conflicting appraisal standards and guidance as well as the inadequate Federal oversight. NAHB believes that fundamental appraisal system reform must be a principal element of efforts to rebuild the Nation's housing finance system.

Coordination and accountability currently are lacking, and there are major gaps in the system. In closing, collateral valuation is critical—is a critical component of the mortgage decision. While there have been a number of positive changes to the appraisal system since the financial crisis, there remain a number of unresolved issues. NAHB stands ready to work with this subcommittee, along with appraisal, housing, and financial stakeholders to address the real challenges we face in restoring the public trust and how we build, transfer, value, and finance America's—American consumers' most valuable asset, their home. Thank you, Mr. Chairman.

[The prepared statement of Mr. Brady can be found on page 40 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Brady.

Ms. Wagner, you are recognized for 5 minutes.

STATEMENT OF JENNIFER S. WAGNER, MANAGING ATTORNEY, MOUNTAIN STATE JUSTICE, INC.

Ms. WAGNER. Thank you, Mr. Chairman, Ranking Member Cleaver, and members of the subcommittee. On behalf of Mountain State Justice, the National Consumer Law Center, and the National Association of Consumer Advocates, thank you for inviting me to testify today.

I am the managing attorney of Mountain State Justice, a nonprofit legal services providers in West Virginia. Since the early 2000s, we have served thousands of the homeowners in danger of losing their homes as a direct result of appraisal fraud and other predatory lending practices. I am here today to thank Congress for imposing stricter new standards for appraisals under the Dodd-Frank Act.

These new standards have dramatically reduced appraisal fraud. In turn, saving countless of homeowners from foreclosure. It is common knowledge that lax regulation of the mortgage and appraisal market led directly to the devastating financial collapse of 2008. Before the collapse, profit-driven brokers and lenders worked with appraisers to fraudulently inflate home values. Lenders made more money from larger loans, and they rewarded appraisers willing to hit target values with repeat business, and sometimes even kickbacks.

Many of these loans contained features that would cause the homeowners' payments to skyrocket after a short teaser period. Even before the market collapsed, consumers and their advocates began to see this house of cards topple as homeowners trapped in these underwater loans were unable to refinance when their payments spiked up. Thousands, and soon millions, of homeowners faced foreclosure. Surely, we all remember this.

In my organization alone, for years, every single week, we saw dozens of homeowners facing foreclosure because of appraisal fraud. Appraisal fraud is why one of my clients, I will call Ms. R, came into my office desperate to save her home. Ms. R had tried to refinance for a lower fixed interest rate after her payments skyrocketed. She was denied because her loan was so underwater and now she faced foreclosure.

How did this happen? A broker appraiser team preyed on her, repeatedly flipping her into loans of ever-increasing amounts. Then a phone salesman for another lender called promising her lower payments. This lender didn't bother with an appraisal. Instead, it used an automated valuation model, which provided a grossly inflated valuation based on flawed data. This inaccurate computer model inflated the value of Ms. R's home by nearly 300 percent. Ms. R was trapped.

The conduct that pushed her to the brink of homelessness also led to the devastation of 2008 when millions of homeowners lost their homes and banks failed across the country. The regulations adopted by Congress in response were absolutely necessary to prevent a repeat of the same devastating events.

The Dodd-Frank Act increased regulation of appraisals building on the necessary safety and soundness requirements passed after the savings and loan crisis. Dodd-Frank has ended the practice of appraisal fraud, primarily by requiring appraisals to be independent as well as accurate and conducted in person by qualified appraisers.

These reforms help homeowners make—help keep homeowners informed about the biggest financial decisions they will ever make. They also protect lenders and investors and insurers by ensuring that they have the collateral necessary to protect their risk. There is no doubt that these reforms have been a success. Weakening these standards, including allowing lenders to rely on alternative valuation models, or eliminating appraisal independence controls, will return us to the recent era of unreliable reports that ultimately upended the market.

The existing baseline of Federal lending and appraisal standards is necessary to ensure that consumers and the entire financial market are uniformly protected from both fraud and from unintentional error. The savings and loan crisis of the 1980s, and then the economic collapse of 2008, showed the urgent need for these commonsense rules.

Eliminating these minimum Federal protections, and instead relying solely on the States would open the door to more economic crises that devastate homeowners and financial institutions alike. In sum, Congress wisely adopted the current Federal appraisal protections to protect the American dream of homeownership and financial stability.

Without these protections, we face the risk of a new financial crisis, even while we barely recovered from the last one. I urge you to keep these essential protections in place. I am happy to answer any questions. Thank you.

[The prepared statement of Ms. Wagner can be found on page 128 of the appendix.]

Chairman LUETKEMEYER. Thank you, Ms. Wagner.

With that, we will begin the questions, and I will recognize myself for 5 minutes.

Mr. Garber, you made a couple of comments with regards to some of the other—the Appraisal Subcommittee and the Appraisal Foundation. I guess, so my question is, do you believe both those entities are relevant?

Mr. GARBER. Thank you for the question. These are two different entities, so I think they should be treated separately, separate discussions altogether. With regard to the Appraisal Subcommittee, we do see that the role that is being played by the subcommittee today has essentially been accomplished as far as its mission and goals.

State appraisal boards have been licensing appraisers for many years, and they are doing a very good job of processing appraisal licenses and certifications, and they are doing a base level of enforcement. This has been going on for some time, and by the Appraisal Subcommittee's own records, they are grading State appraisal regulatory agencies very well. There is no State that is at risk of compliance burden.

The issue with the Appraisal Subcommittee is that it is set up by FIRREA, which the way it is structured, it results in an ever-increasing set of regulations on top of appraisers. It is an oddity in the—

Chairman LUETKEMEYER. That begs the questions then, do you believe the regulatory system for appraisers needs a Federal regulatory body?

Mr. GARBER. We think that the Federal role should be repositioned to that of a last resort. So right now, the Appraisal Subcommittee is odd in that it actually audits independent or sovereign State agencies. We find no comparable for this in the marketplace today in any regulatory aspect where the Federal Government is actually auditing State agencies. So we are suggesting that that be aligned with those that—recent precedents that have been enacted by Congress, like the NMLS, which puts the burden on the States, the States have to maintain that job, and as long as they are performing at a high level, then they are allowed to do that, but there is still a Federal role, but it is one of a last resort.

Chairman LUETKEMEYER. Okay. Mr. Park, would you like to respond to that?

Mr. PARK. Sure. The regulatory system that we have in place now recognizes States' rights, and what the Appraisal Subcommittee does in terms of our compliance reviews of the States is we review the States to make sure that they are in compliance with Title XI, which includes the AQB minimum criteria, that they have implemented USPAP, and that they are in compliance with those minimum baselines.

Again, it is key to have that minimum baseline for the States to adhere to in order to facilitate commerce. Otherwise, without that minimum baseline, you are going to have the States go in 55 different directions, and it is going to increase the cost and burden on mortgage lending significantly.

Chairman LUETKEMEYER. Okay. I had a very good friend of mine, who is an appraiser, and I had a long conversation with him just last week, and his comment to me was that he didn't know how any person could ever get started in the appraisal business today, because of the difficulty of getting licensed and finding your own business.

The business model is not—and I come from rural Missouri. I am about as rural as you get, a town of 300 people, but he lives in a town of about 30,000. But the problem is, as a number of you indicated here, that there is a shortage. There is a shortage in my area. And while I recognize 2008 pointed out some problems, has Dodd-Frank caused—the rules that came out of Dodd-Frank, have they—has the pendulum swung so far that now we are lining up with a shortage? That the restrictions in Dodd-Frank are such that it is squeezing the appraisal industry to the point where we don't have people being able to get in it? And if so, that is a problem, and how do we fix that? Excuse me. One of you want to tackle that? Mr. Bunton?

Mr. BUNTON. A couple of issues regarding the shortage. One, Dodd-Frank and regarding the appraisal management companies, I think a lot of lenders felt that they were compelled to establish appraisal management companies. And what has happened is because of their focus on—a lot of them. There are good AMCs, but a lot of them are not maybe not as good. They focused on the cost and the turnaround time. So there is a shortage of appraisers who are willing to work for that fee. We still have a lot of appraisers. We have more certified appraisers today than we did 10 years ago, but they don't want to work for that fee.

The other impact is, is that the licensed appraisers in the United States, when FHA, through an act of Congress, said that we can only use certified appraisers, that had a huge impact, particularly in rural areas where you had licensed appraisers. The number of licensed appraisers—excuse me, 10 years ago, there were 29,000—just under 30,000. Today there are 7,900, and so there has been a huge drop in the licensed category.

Lenders don't want to use licensed appraisers or trainees, and that creates the problem that your friend talked about entering the market. Banks used to be the training ground for appraisers. Now they have outsourced it, and since banks don't want to use trainees or licensed people, people don't want to bring on trainees because they are not really good. Thank you.

Chairman LUETKEMEYER. Very good. I appreciate your comments. My time has expired. With that, we recognize the gentlelady from California, Ms. Waters.

Ms. WATERS. Thank you very much, Mr. Chairman. Today, we are examining proposals to fix our current system of regulating and overseeing appraisals, but is there really any reason to believe that it is broken?

To the contrary, it seems that we have substantial evidence to demonstrate that our current system, in particular, the important reforms brought about under Dodd-Frank, has been largely successful in streamlining standards across the country and protecting us against the kind of harmful appraisal fraud that we saw leading up to the housing crisis.

While there is always room for further improvement, I don't see any reason for a complete overhaul of our current system as some have suggested we need. So I would like to get some comments of Ms. Wagner. Freddie Mac recently announced that it plans to dispense with traditional appraisals for some mortgages and replace them with automated valuation models, AVMs. Further, Mr. Park's testimony supports the use of different valuation products, according to the risk characteristics of a loan.

Can you talk about some of the risk that AVMs can impose to consumers and the financial system? Do you think that AVMs could be appropriate for some lower risk loans, as Mr. Park has suggested?

Ms. WAGNER. Thank you for that question. First of all, I do agree that, as they say, "if it is not broke, don't fix it," and I don't think that we are broken. In fact, I think that we are engaged in fixing what happened before.

AVMs do give me significant concern, and they give the appraisers that I have talked to, as well as my homeowner clients, those same concerns. They just can't be fully accurate. If you use a computer valuation model, you are not getting the input of actually going out to the house and seeing whether there has been any kind of damage to the interior of the house, and you are also not getting the input of if someone has made substantial improvements to the house.

There is no standardized method for AVMs, and a lot of the data inputs are simply inaccurate coming from tax data that is outdated, and from the use of comparables not based on actually seeing whether those properties are comparable, but just sort of inputting from the area. And a lot of places, there is tremendous diversity in housing. It is not just subdivisions.

And one example is a client of mine, who lived on a road right next to a subdivision, an appraiser in that case used comparables from the subdivision that were much closer to her house than houses that were actually much more like her house. An AVM model would do that same exact thing without any kind of oversight, so you can't see the property appeal, you can't see the unusual characteristics of the property, you can't see any kind of damage, infestation of rats, anything like that, and you can't see any kind of improvements, so it does greatly concern me.

Ms. WATERS. Well, thank you very much, and I believe exactly what you said. First of all, I like independent appraisals. I like small businesses. I don't like the way the system may be run now with the management, appraisal management companies and taking a fee or cut, you know, from the appraisers. But let me ask you, because I think there is room for dealing with still some potential fraud.

If the lending institutions are owning still some of these appraisal units in their business, I think that is a problem. I would like to get rid of that. But let me just, you know, agree with you in saying that the work that was done in Dodd-Frank really did get rid of a lot of the problems, a lot of the fraud. I see no reason at all to be talking about getting rid of Dodd-Frank.

With all due respect to Mr. Luetkemeyer, you are absolutely right. There is no way that these models, these AVMs can determine what that house really is, what it really looks like, where the damage is, et cetera, et cetera, and again, I think as I was coming in, I heard some testimony from someone that talked about the recent big data problem that we are seeing in the election, and on and on and one. Get rid of that crap. Leave the human element in appraisals.

And so with that, thank you for your testimony here today. I agree with you 100 percent, and I yield back the balance of my time.

Chairman LUETKEMEYER. The gentlelady yields backs. With that, we go to the gentleman from New Mexico, Mr. Pearce, for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman. Mr. Bunton, where does the Appraisal Foundation get its funding?

Mr. BUNTON. The majority of the funding is through publication sales, the book of standards course work, material like that. We receive a grant from the Appraisal Subcommittee for $350,000, the current grant level, and our budget is about $4.2 million.

Mr. PEARCE. Okay. Mr. Park, you heard Ms. Wagner's testimony and said that basically the bubble in the housing prices were not created by spiking—just by a spike in consumer demand, but as a result of intentional fraud and lack of oversight. So that seems to be sort of directed at your function to me.

I mean, I am—I have to confess, I am a little bit confused by—I think as Ms. Trice's chart shows, so I am a little confused about what is going on, but—so is her statement a reflection of the oversight that you bring?

Mr. PARK. Well, her statement reflects the States are the one that regulate appraisers—

Mr. PEARCE. Yes, but I know, but you—

Mr. PARK. —directly

Mr. PEARCE. —you oversee the States, and you are supposed to—it says in your document that you can bring actions if a State is in noncompliance. So surely, the Federal Government doesn't say that it is okay to create fraud and the States don't say it is okay to create fraud, so you would expect there would be something that would show up if the amount of fraud is there. So I am just asking, is that a fair assessment of your oversight?

Mr. PARK. The Appraisal Subcommittee's role is to oversee the States in regard to—

Mr. PEARCE. Okay.

Mr. PARK. —requiring—

Mr. PEARCE. Sir, with all respect—

Mr. PARK. —to Title XI.

Mr. PEARCE. You oversee the States, but you say on page 8 that you have the right to bring action in the case of noncompliance or order of nonrecognition. Does that mean that you don't have oversight of the States? You don't—

Mr. PARK. We do have oversight of the States.

Mr. PEARCE.And you can't do anything about it.

Mr. PARK. We would take action if a State is in—is not complying with Title XI.

Mr. PEARCE. So you are saying the fraud that was—the fraud that was suggested by Ms. Wagner was then approved under Title XI. That is what I would have to draw the conclusion, if you don't find any reason to bring an action. It says you have the right to bring the action in your own document.

Mr. PARK. Generally speaking, if there is a fraudulent appraisal, there is going to be a violation of Uniform Standards of Professional Appraisal Practice, USPAP, involved in that fraudulent activity. The States are the ones that handle complaints and adjudicate complaints in regard to fraud in their State or violations of the uniform standards.

Mr. PEARCE. So if there is fraud going on that was alleged there, then you have no say-so.

Mr. PARK. We have to work within the purview of the law.

Mr. PEARCE. So what does—have you ever brought an action against the State?

Mr. PARK. We have never taken a nonrecognition action against the State, which, prior to 2010, the Dodd-Frank Act was the only action that the subcommittee could take against a State, which would be a very dramatic and Draconian action. The subcommittee has chosen, for the past 25 years, to work through the partnership with the States and with the foundation to correct—

Mr. PEARCE. But you are never taken an action?

Mr. PARK. —a problem within—we have not taken—

Mr. PEARCE. You have not taken an action, and yet, according to Ms. Wagner, fraud was the reason for the bubble in—

Mr. PARK. And the Dodd-Frank Act gave the subcommittee additional regulatory authority to take actions in lieu of, or short of a nonrecognition—

Mr. PEARCE. You have gotten that—

Mr. PARK. —process.

Mr. PEARCE. You have gotten that additional permission, and have you done anything under that?

Mr. PARK. We have not found—

Mr. PEARCE. Okay. That's all I need to know.

Mr. PARK. —the need to take any further action.

Mr. PEARCE. Ms. Trice, would you like to address this, because this seems like no one is in charge of anything, that we are going to oversee but we are really not going to take any actions. Would you like to make an address on this?

Ms. TRICE. Yes, please. I think the consumer is the one who is the one who gets punished the most by this regulatory structure that I have diagramed here. So if a consumer has a problem with the appraisal, and the NAHB pointed this out as well, if someone needs to make an appeal, there is not an efficient, effective process. So if it is immediate, let's just say there is an appraised value falls short of the contract price, the consumer can only make an appeal to the lender. If they make an appeal to the State—

Mr. PEARCE. Let me ask one more question, if I can.

Mr. Garber, in your opinion, what would happen if AFC didn't exist at all?

Mr. GARBER. Well, if States would continue to do licensing and enforcement—but we are not suggesting that that go away.

Mr. PEARCE. I didn't ask. I am asking for my perspective, and my time is about shot.

Mr. GARBER. Yes. From right now, the appraisal community would have a less burdensome regulatory environment. In fact, it would be a more attractive proposition to enter the profession because we would have fewer rules and volume of layering effect that is currently occurring under the current regime.

Mr. PEARCE. Okay. Thank you.

Mr. GARBER. That is important to the rural markets.

Mr. PEARCE. All right. Thank you. Thank you, Mr. Chairman, for your indulgence.

Chairman LUETKEMEYER. The gentleman's time has expired.

With that, we go to the gentlelady from New York, Ms. Velazquez.

Mr. VELAZQUEZ. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. You are recognized for 5 minutes.

Ms. VELAZQUEZ. Thank you. I would like to address my first question to each member of the panel.

Given that automated valuation models are playing an increasing role in residential valuation and the number of appraisers is dwindling, the appraisal landscape is changing quickly, regardless of regulation. What do you see as the role of appraisers 10 years from now? Mr. Park?

Mr. PARK. The appraiser profession is still and will continue to be a very important cog to the financial system in the United States. Automated valuations, automated tools can only go so far. You don't realize how big this country is and how diverse the housing is in this country until you start trying to place appraisal orders all over, all over the Nation.

Ms. VELAZQUEZ. Uh-huh.

Mr. PARK. There are certain areas where you have homogenous property types where automated tools are useful, but I would submit that those tools should not be left alone so that a computer is generating the valuation without—without an appraiser's expertise being involved.

So the future is, appraisers will have to adapt to uses of technology, lenders will have to adapt, and so will regulators.

Ms. VELAZQUEZ. Thank you. Mr. Bunton.

Mr. BUNTON. Automated valuation models are a tool that appraisers use. That is all they are. And there may be an application for them, as Mr. Park points out, with homogenous housing stock, with a very low loan-to-value, those types of things, but as far as 10 years from now, you are still going to need a valuation professional to sift through all the data.

They will probably perform more appraisals in a day than they do today because they will have access to a great deal of information just sitting at their desk, but you are going to need that human interface of a trained valuation professional to make determinations, particularly in areas where you don't have a homogenous housing stock.

Ms. VELAZQUEZ. Thank you.

Ms. TRICE. There is two basic components to an AVM. One is the data, the second one is the algorithm. So today, we have a very poor database, frankly. We have no inventory of every piece of property in the United States, so we have MLS data, which is essentially sales data, which is, how do I say, flowery sometimes. It is not necessarily factual. Then we have public record data, which varies from State to State and county to county, so in essence, we don't have very good data.

In theory, AVMs in the future could become more reliable, but today's market, they are not. And just a reminder, human beings write the algorithms, so it is nothing more than an opinion cloaked in a mathematical formula.

Ms. VELAZQUEZ. Thank you.

Mr. GARBER. Thank you for the question. Big data, in general, has the potential to enhance the valuation process if it is looked at closely, and there is a trained professional evaluation of the methods that are used.

Right now, there are appraisers that are integrating big data into their own appraisal reports, and I think you would find, may be surprised that a lot of appraisers are actually very technologically savvy today.

I think our biggest concern is we don't see that our regulatory structure is really positioned to allow and enable appraisal professionals to provide the full range of services that the user community and consumers really are looking for. There is a full range of demand for valuation services. Loan purchases is a big one, but it is not the only one. You have refis, you have workouts, you have the ability or the need to do monitoring of entire portfolios.

Right now our estimates indicate that there are four evaluations performed for every single appraisal in the market today. Right now appraisers are not involved in the majority of the valuation services that are being engaged by financial institutions.

We want to position our regulatory structure so that it is more responsive to those needs.

Ms. VELAZQUEZ. Thank you.

Mr. Brady.

Mr. BRADY. Just very quickly. Data is important, especially in our segment of the industry in new construction. It changes every day. It relies on code changes, it relies on energy and efficiency. So the human touch is always going to be an element.

I think the AVM is a resource. But we should not rely, especially in our segment of the market, on AVMs.

Ms. VELAZQUEZ. Thank you.

Ms. Wagner.

Ms. WAGNER. Very briefly, I do think I addressed this question a little bit. But I think looking ahead into the future, it just highlights the need for careful regulation in a Federal structure in order to ensure that there is some consistency and safety in the marketplace. So if we do end up using these models slightly more, it should be balanced with actual appraisals, and we do need some oversight to make sure it is done fairly and safely for everyone.

Ms. VELAZQUEZ. Thank you.

Thank you, Mr. Chairman.

Chairman LUETKEMEYER. The gentlelady's time has expired.

We have a great discussion going here today. I thank all of the panel for their concise answers.

With that, we go to Mr. Rothfus from Pennsylvania, for 5 minutes.

Mr. ROTHFUS. Thank you, Mr. Chairman.

Mr. Garber, while I understand that a national appraiser shortage may not yet be here, though industry trends suggest that one may be coming soon, we all seem to agree that localized shortages are a problem, especially in rural communities. My district includes a number of rural communities and I was hoping to get a better understanding of how this dynamic may impact my constituents. Can you describe how localized appraiser shortages may impact communities such as those in rural Pennsylvania?

Mr. GARBER. Yes, thank you for the question. Appraisers, as I was saying, are facing a layering effect of rules and regulations right now, and it is never ending at this point, where there are no bounds around the current regulatory structure.

So as an example, we have seen proposals and actually in effect now programs to codify appraisal methodology, where appraisers not just have to follow a certain standard, but are being obligated to follow methods and techniques, such as the cost approach or the sales comparison approach or the income approach in the appraisal process, and follow it along a strict guideline.

Mr. ROTHFUS. Where would that be coming from?

Mr. GARBER. Well, it came from a proposal originally directed by the Appraisal Subcommittee for The Appraisal Foundation to undertake, and that has resulted in the creation of a third board under The Appraisal Foundation called the Appraisal Practices Board.

That board has a very unclear role in today's marketplace, but I will give you an example of how it is being used. State regulators have already identified this as a document or a set of materials that they are using in enforcement cases. So appraisers have to keep that in mind as they are developing their appraisals.

And just last week I was talking with an official at Freddie Mac. Freddie Mac issued a bulletin last week on green and energy-efficient appraisal issues. Within that bulletin, those documents are actually referenced.

In talking with the Freddie Mac official they indicate that those bulletins are actually part of the contracts that they have with loan sellers to Freddie Mac. Those are now effectively part of the contract when a lender sells a loan to Freddie Mac. They don't realize it, but that is an unauthorized board of The Appraisal Foundation today, but their lenders are going to be obligated to follow all of that information to a tee.

And in your rural market, every market is different, so the rules or the guidelines that work in Washington, D.C., may not work in rural Pennsylvania, because every market is going to be different. That is why we need to have more flexibility to the methodology.

Mr. ROTHFUS. Would you think that if you are seeing some shortages appearing in some areas, rural areas, could those trends eventually get to other areas.

Mr. GARBER. So absolutely. I provide some information on the projections ahead. We do see the potential for a 20 to 25 percent continued reduction or a further reduction over the next 5 to 10 years.

What is troubling to us is that there are fewer appraisers that are interested in entering the profession. They are facing all of these rules, regulations, fees. Right now, the Appraisal Subcommittee is about ready to finalize a rule to implement an appraisal management company registry fee. The process that was used to undertake that rulemaking failed to consider the impacts on small businesses.

The reality is that rule is going to impose significant fees on small business appraisal service providers, because they are going to be passed through from the appraisal management company directly onto the heads of practitioners.

If you are an appraiser, you are looking at this system, you are stepping back and you are reconsidering the proposition today. And that is what troubles us as a leader within the appraisal profession. We need to reposition this to make it a more attractive endeavor.

Mr. ROTHFUS. Thank you. Move over to Mr. Park.

Alternative valuation models or methods have been used by the appraisals industry for many years. In your testimony you seem to support the use of new methods and new technologies based on improved data, yet you caution against moving completely away from an appraiser-based process. Could you describe for which types of transactions alternative valuation methods, such as automated models, might be most appropriate?

Mr. PARK. Yes, thank you for the question.

As I stated earlier, in areas of the country where you have a more homogenous housing stock, where you have good quality data, coupled with a low risk transaction—when I say a low risk transaction, an example would be a rate and term refinance where a borrower is simply lowering their rate from 5 percent to 4 percent, something like that. They are not taking cash out. There is no additional risk in the transaction. The borrower has a good credit score and so forth. They pose a good credit risk with little likelihood of default. Those are transactions where an AVM could be useful again with human intervention in terms of making sure that the results of that AVM make sense.

Mr. ROTHFUS. I yield back. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman yields back.

With that, we go to the ranking member of the committee, Mr. Cleaver from Missouri.

Mr. CLEAVER. Thank you, Mr. Chairman.

Ms. Trice, do you like hamburgers.

Ms. TRICE. Excuse me?

Mr. CLEAVER. Do you like hamburgers?

Ms. TRICE. Hamburgers? I love hamburgers.

Mr. CLEAVER. Do you prefer mustard or mayonnaise?

Ms. TRICE. Neither.

Mr. CLEAVER. Neither. What do you prefer?

Ms. TRICE. I like ketchup.

Mr. CLEAVER. Ketchup. I don't. But I delivered a speech in actually the boot heel of Missouri, Cape Girardeau, which you may or may not have heard of. So I go to Chili's and I sit at the table with a staffer and there is no waitress, there is no wait staff at all. They have a contraption on the table. It says, place your order. And it came with mustard, and I like mayonnaise. I think that is one of the great tragedies of this moment.

And so I think that there is some general consensus that the AVMs or the new technological way in which some of these appraisals are done, particularly, I guess, with home equity loans, primarily with home equity loans, but I think you can also sense that there is some concern here about that.

And so I am wondering, you know, I don't want to be a troglodyte and I am afraid of technology, you know, but what happened in the financial crisis is that the appraisals ended up being far too generous. And so I think in some instances people thought, well, you know, if we can put the AVM it will stop that process. But it also removes the humanity from it. It also creates some other issues.

So, you know, any time we have come up with a new technology, a great technology, I think, and I am looking for this, too, that there has to be some kind of counterbalance to maintain the humanity. And so I am wondering if most of us agree that the system is somewhat flawed right now. What can we do as a counterbalance?

Ms. TRICE. One of the problem with AVMs is that they can be manipulated and we saw that in the mortgage crisis. So what happens is they built what they called cascades so that they would bundle 10 different AVMs into one ordering platform. Well, what would happen is a lender would continue it order an AVM until, bingo, he got the number that he needed.

So one of my dear friends was an AVM developer, and he had sold his company, and the entity that bought his company said, hey, we need to juice the algorithm, because in Florida we are not getting enough hits, so we need you to dial in a 20 percent appreciation rate in Florida. Because they are only get paid if they get a hit on that AVM. So don't for a minute think that AVMs can't be manipulated and subject to fraud.

Mr. CLEAVER. Oh, yes.

Ms. TRICE. They just can do it on a wholesale basis rather than one at a time.

Mr. CLEAVER. Mr. Brady.

Mr. BRADY. I think it is an overall—I mean, reform is needed. The Appraisal Subcommittee as example probably doesn't have enough teeth. They talked about it earlier, there is no enforcement. I mean, you can note a problem in a State, but they need a little bit more authority to take action.

From State to State is different. Some have boards, some have funding, some don't. Some sweep the funding on appraisal fees into the general fund and don't fund it appropriately. So there needs to be a better standard.

The appeals process, we need a good appeals process, because I had an example just 3 weeks ago where I had a plan, new construction. I gave them a cost analysis, $249,000, it came in at $234,000. The reason it came in at $234,000 is the oversight of not finishing the basement and 9-foot ceilings. Very simple, yet I wasn't able to convince that appraiser to make that change.

So we need a very quick and adequate appeal process to at least not inflate the cost, but justify the cost.

Mr. CLEAVER. Is that something we should be doing?

Mr. BRADY. There should be a standard within the industry, like the VA, like the Tidewater potential, the Tidewater Initiative, that allows an appraiser to call if it is undervalued compared to what the contract might be, to call and ask questions. And we have gone so far away from that because of political correctness and worries that we are inflating the price of a product valuation that we have gone, as the chairman suggested, the pendulum has swung almost too far to really punish the supply or the provider.

Mr. CLEAVER. Thank you.

Chairman LUETKEMEYER. The gentlemen's time has expired.

With that, we will go to the gentleman from Kentucky. Mr. Barr is recognized for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman.

Thanks to our witnesses for your testimony.

I was particularly interested in Ms. Trice's appraisal oversight schematic or graph that shows the complexity of the oversight system that we have in place now and interested in your suggestion of a big and bold plan to overhaul the system.

I do think that that you are right, that sometimes less can be more in terms of actually providing for an accountable system, because when you do have this dizzying maze of agencies and responsibilities you are dividing lines of accountability and the responsibilities of the participants are not clearly set forward.

So can you just summarize your testimony a little more and amplify it to say what would be that big and bold plan that would streamline the system? And do we still need the ASC, the subcommittee, or does it need to completely replaced with a new structure that you are proposing?

Ms. TRICE. Well, I do call for a new structure, but that doesn't mean that you wouldn't take the components that do work from the current system and put it in this new entity. I mean, we do need licensing of individuals.

Lending however is national, it is no longer local. And so if we set up a 50-State system, you essentially are—I will borrow from this President-elect Trump—we are building a wall between each border of each State.

So we have to have a system that is portable across all States and it is uniform in its standards, so if I get a mortgage in Maryland and I want to move to Delaware I know exactly what to expect and the process is uniform.

I do subscribe to the theory that people are honest and want to do the right thing, but under the current regulatory scheme, they don't even know what the right thing is to do. So, you know, it certainly is difficult to follow the rules when you don't understand the rules and whose rules they are.

Mr. BARR. Has the Dodd-Frank law helped proliferate the complexity of the regulatory structure or are there some positive changes there? What is the impact of Dodd-Frank in exacerbating the complexity?

Ms. TRICE. Dodd-Frank has many positive components. Number one, the appraisal independence requirements are really critical to the appraisal process. The problem has actually been the enforcement of it.

So we keep adding new regulations, but we didn't enforce any of them. So the result of that is we punish good people and the cost of compliance has just gone off the charts. But bad actors continue to behave badly.

Mr. BARR. One thing I keep hearing from constituents, banks, actors in the real estate market, is that there are excessive appraisal requirements that add unnecessary costs to transactions, and I would like for any of you all to comment on that.

In other words, the complaint that I am hearing specifically is that there are new requirements, I don't know if they are Dodd-Frank requirements or other regulatory retirements, that require appraisals every time there is a refinancing or every time there is a transaction, even when there is not a material change in the valuation of the property.

Can anybody speak to that of what is the cause of that? And do we need as many appraisals as we have?

Mr. GARBER. Well, we just got through a bank crisis, so that is partly what is going on there, is that we have a lot of failed banks or banks that have been coming up for air. And so the bank examiners have been monitoring, they have been examining those cases, looking at those portfolios, and they have seen a need to kind of get an understanding of the risks that are involved there.

So having an appraisal to update those files, to understand your risks from a taxpayer standpoint is an important thing, and I think that is a good goal from a safety and soundness standpoint. But from the appraiser's standpoint, there are clearly new rules that are hitting appraisers on the head. We see fees that are being passed through to appraisers to be paid for in order to be accepted on an approved list.

I mentioned the registry fees that are coming from the Appraisal Subcommittee. That is going to hit appraisers squarely in the face and be a huge disincentive from practicing in those areas.

And financial institutions themselves, too. People don't realize there are a lot of appraisers that work at banks. Bank appraisers have to deal with this complicated regulatory structure, too, and they have to obtain those licenses just as the practitioners do. So an efficient system would be helpful there.

Mr. BARR. Thank you.

Chairman LUETKEMEYER. The gentleman's time has expired.

I now recognize the gentleman from Texas, Mr. Green, for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman.

I thank the witnesses for appearing as well.

Mr. Brady, I was especially interested in your comments. If you might recall, when I gave my opening statement, I dealt with this area of appraisals and appeals, and you have followed up on this.

Let's just talk about a possible example to make this clear, or clearer, if we can. Let's assume that you have an FHA loan and the seller believes that there is a problem with the appraisal. I won't use terms like fraud, but there is a problem. And let's assume that the buyer thinks there is a problem as well. What is the process at that point to allow them to have an opportunity to impact that appraisal?

Mr. BRADY. Well, it varies, and a banker that gets an appraisal that doesn't meet a contract price can ask the appraiser to talk to the seller and try and justify it. Many times that doesn't occur and that is where the problem exists.

But also, in a transaction where you get an appraisal a week before, let's be generous and say a week before closing, and the appraisal's not justifies the purchase price, that process takes much longer, the deal either blows up, doesn't close, both buyers or sellers are unhappy.

In a new construction situation, many times sellers, meaning us, will eat the difference, not justifiably, but in order to close a house because the appeal process or that process is too lengthy to get it done in a matter of time. So where it would take place better is in the Tidewater Initiative where an appraiser would conduct the seller prior to issuing an appraisal, so that they can either justify or not, not inflate the price, the purchase price, so that it doesn't happen at the last minute.

Mr. GREEN. I understand. But is that required, is it required of the appraiser to have that conversation?

Mr. BRADY. No.

Mr. GREEN. And in a good many cases that does not happen is what you are saying?

Mr. BRADY. That is correct.

Mr. GREEN. Now you indicated that you sell properties, obviously you do, you are a builder. But let's just take the homeowner who just has a home, a typical person in the United States America. If this person finds problems with the difference, that person may not be able to eat, that was a term you used—

Mr. BRADY. That is correct.

Mr. GREEN. —to eat that loss. That person my find it unacceptable. At this point can that person go out and say, ″Well, let me just get another appraisal″?

Mr. BRADY. No. I don't believe they can go out and get another appraiser appraisal.

Mr. GREEN. Believe you are right.

Mr. BRADY. But time is of the essence and they don't have time to justify the actual cost.

Mr. GREEN. Well, it is not just the time. There are other factors involved, too.

Ms. Wagner, your hand has been up. I would like for you to respond quickly, if you can, please.

Ms. WAGNER. Yes, thank you.

One concern that we do have with the appeal process is that, while there might be some legitimate cases where we have seen that type of process manipulated in the past that has led to overvaluations, we have seen lenders contacting appraisers and pressuring them to increase values or telling appraisers that the values have come in too low, and then there has been some manipulation within the system to then come back with a higher value.

Mr. GREEN. Let me intercede for just a second. So we are concluding that we need a balance.

Ms. WAGNER. Right.

Mr. GREEN. And there seems to be a pervasive belief that that balance has not achieved, and that is what I want to work on, to try to achieve that balance. I would like to work with you, Ms. Wagner—I also want to work with you, Mr. Brady—to see if we can achieve that balance, because that is what is critical.

And the realtors are telling me that balance has not been achieved. I have talked to homeowners who believe that it hasn't been achieved, because once they get the first appraisal, getting another one is not an easy thing to accomplish. I think there is a waiting period before you can get another appraisal. Is that right, Ms. Wagner?

Ms. WAGNER. That is true for FHA loans.

Mr. GREEN. FHA, yes. Is that waiting period about 6 months?

Ms. WAGNER. Yes, sir.

Mr. GREEN. Okay. So you are stuck with a 6-month appraisal. You are a homeowner, you are not a builder, you don't eat losses. You are trying to move up in the world. So I want to correct this.

But let me quickly say this, I want to move to another area. None of you are here today to say that we should get rid of Dodd-Frank because of your concerns and the consternation that you have with one area of it. Is that a fair statement? Are you here to say you want to eliminate Dodd-Frank? Anyone? If so, kindly raise your hand. All right.

Now, I want to go to one specific area of Dodd-Frank. We have a Defense Department in this country. We have a Securities and Exchange Commission to protect investors. The Defense Department defends the country. Why wouldn't we have a Consumer Financial Protection Bureau to protect consumers? Anybody here want to get rid of the CFPB today? If so, raise your hand. Do you think that it is just a horrible institution and we ought to just do away with it?

Thank you, Mr. Chairman. I yield back the balance of my time. No hands raised, for the record, on either question. Thank you. I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired.

We welcome Mr. Sherman to the committee today for some questioning. I see he is here and wants to participate. So we welcome him. The gentleman from California is recognized for 5 minutes.

Mr. SHERMAN. I thank the Chair for letting me participate, although I am not a member of the subcommittee.

I would like to ask The Appraisal Foundation how close you are to releasing new rules for entering appraisers.

Mr. BUNTON. We are currently in the—we call it the exposure draft process. Much like regulators, we issue drafts. We want to make sure we get it right. That board that does it actually has a meeting this Thursday and Friday in St. Louis. My guess, it would probably be spring before it occurs.

Mr. SHERMAN. I will ask this of whatever witnesses would choose to respond. What are one or two facets of the current appraisal system and system of appraisal regulation that you think we ought to preserve that are essential regardless of what other changes might be made?

Mr. GARBER. I would be happy to take that, Congressman. The Dodd-Frank Act anti-coercion provisions and the appraisal independence provisions of Dodd-Frank are extremely important. I remember living the era of the housing boom, and I think we were on record to Congress with a letter of caution, a pending house of cards, as early as 2002. So those protections are important.

I would point out that those are part of the Truth in Lending Act. They are not part of FIRREA. So when we are talking about making changes to our regulatory structure, we are really referring to the FIRREA, the original FIRREA statute, and less so relative to Dodd-Frank, particularly those anti-coercion provisions.

Mr. SHERMAN. Mr. Brady.

Mr. BRADY. I would just follow up.

The independence is a good thing, being able to have independence from appraisers. But the problem is you put all your eggs in that one basket, on the independence on the AMCs, as some of the panel suggested, we are getting less qualified, less educated, less trained appraisers sometimes in those AMCs. That creates a problem that we have to resolve at least by an appeal process, in a very thorough and expeditious appeal process.

Ms. TRICE. I reiterate appraisal independence is the most important component of Dodd-Frank.

Mr. SHERMAN. Mr. Bunton.

Mr. BUNTON. If I could just speak to that.

Appraisal independence is a great thing. Unfortunately, it also has caused sometimes appraisers to be viewed as radioactive, where real estate agents don't want to talk to them because they are afraid they are going to get in trouble, lenders doesn't want to talk to them.

As the gentleman was talking about earlier, you need that communication between the appraiser, and whether it is the lender or the real estate agent or the homeowner, so that he has as much information. Talking to an appraiser is not coercion. It is communicating. It is giving information.

Mr. SHERMAN. Thank you.

What can be done to encourage appraisers to work in rural areas to address supply issues?

Mr. Garber.

Mr. GARBER. Well, make it make their lives easier for one. More productive and profitable would be helpful. Stop imposing new rules and mandates on how they do their job relative to the methodologies in particular, because those rural areas are very complex.

An appraisal in Washington has vast amounts of data, you have a lot of conforming markets. Whereas in a rural area, you might have data access problems and there might be limitations with the data.

But the notion of trying to codify the appraisal process, including the methods that they are using, how to use the sales comparison approach, as an example, in those markets, that is a disincentive to entering the profession. That is why appraisers enter the appraisal profession, is because they are paid to provide their professional expertise. They are trained, they know appraisal and valuation, and they should be allowed to do their jobs and use their professional judgment, not follow a set of rules like a cookbook.

Mr. SHERMAN. I understand.

Let's hear from Ms. Wagner.

Ms. WAGNER. I think that these overarching standards are actually really necessary for appraisers. And I have worked with many appraisers in my largely extremely rural State of West Virginia, and the regulations have never been and the USPAP standards have never been addressed to mean, by honest, hardworking appraisers, they have never said that there is a problem with the USPAP standards.

There is room within those standards for rural communities, for areas like this, and there is a real need to have that guidance. And so, that is something that I have heard from appraisers who want to do the right thing, and any kind of flexibility with that would be used by the dishonest folks who want to get away with something, is my understanding from that market.

Mr. SHERMAN. I want to sneak in one other concept. Should we change the rules to allow interstate work more easily?

Yes, Ms. Trice or Mr. Park.

Ms. TRICE. In specific to commercial work, definitely. If I am an expert in appraising a golf course, for example, and I am on the East Coast, and I get called—there aren't that many golf courses in the United States—I have to apply for a license.

Mr. SHERMAN. I hear the administration is going to see to more. But go on.

Mr. PARK. There are already rules in place for appraisers to be able to apply for reciprocity between States. And that process has become much smoother and much better over the last several—

Mr. SHERMAN. I believe my time has expired. I thank the chair.

Chairman LUETKEMEYER. I thank the gentleman.

We have a second round planned here. The gentleman from New Mexico has some very salient points he would like to make. He is recognized for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

Ms. Trice, I don't mean to be picking on you, but you seem to be kind of a straight shooter. So from this side of the aisle, from this side of the table, when I read the statement by Ms. Wagner, and I am kind of wanting you to help me evaluate that. It says, "It is common knowledge," page 2 of the testimony says, "It is common knowledge that lax regulation of the mortgage and appraisal market led directly to the financial collapse of 2008. Prior to the collapse, unscrupulous mortgage brokers and lenders joined forces with a handful of appraisers to fraudulently inflate home values."

So from my perspective looking at a thing that runs into the hundreds of billions of dollars and maybe nibbles into the trillion-dollar range when you look at home values, is it possible for a handful of appraisers to have done that?

Ms. TRICE. No, not all by themselves.

Mr. PEARCE. Okay.

Ms. WAGNER. If I may actually respond to that. I mean, since you are using my language.

Mr. PEARCE. Well, I appreciate it. I am just reading your statement.

Ms. WAGNER. I know, and I would be like to be able to clarify.

Mr. PEARCE. Mr. Park, actually I really want to direct myself now to the time element that Mr. Green got into. So when you all are checking the States out, do you measure the time from the initiation? Do you get sort of a trend across the Nation that this State takes 1 day, this State takes 6 months, or whatever? Do you do that kind of analysis?

Mr. PARK. In terms of handling complaints?

Mr. PEARCE. No, no, no. The terms of the appraisal process, how long it takes.

Mr. PARK. No, that is not something that the subcommittee has the authority to delve into in terms of the States.

Mr. PEARCE. Okay. But you do keep a registry of people, of appraisers.

Mr. PARK. We maintain a national registry of appraisers who are eligible to perform appraisals for Federally related transactions.

Mr. PEARCE. Okay. And so Ms. Trice made a comment that bad actors continue to act badly. Do you ever take people off of that registry? And what is the process by which you take them off?

Mr. PARK. We do. In cases where appraisers are found to be not compliant with the requirements we will remove those. In limited cases those appraisers can be removed from the registry.

Mr. PEARCE. And you take the States' information for who is compliant and who is not or you track your own compliance and noncompliance?

Mr. PARK. We take the information from the States. The Dodd-Frank Act also gave the subcommittee additional authority to remove appraisers and AMCs from the national registry on an interim basis in lieu of States failing to act.

Mr. PEARCE. So again, going back then to the assertion that the appraisers were a key piece of the collapse of 2008, how many appraisers did you pull out of your registry for bad acting?

Mr. PARK. Again, we haven't pulled off any appraisers on a permanent basis for bad acting, as you put it. Regulation of appraisers resides within the States.

Ms. PEARCE. I understand, but you are the one that keeps the registry. That is what your paper says. And you said you had taken people off the registry. So my question is, how many have you taken off the registry?

Mr. PARK. The registry is populated by the States. The Appraisal Subcommittee does not enter the data into the registry.

Mr. PEARCE. It says the ASC is required to maintain the registry?

Mr. PARK. We maintain the database and the States populate it.

Mr. PEARCE. All right.

So one of the things in your testimony that you do say is that you are in the process—or one of the things that is greatly needed is to streamline processes, streamline and stabilize the appraisal standards. Now, is that something you all have attacked or is this something you just identified that needs to be attacked?

Mr. PARK. It is something that we have identified as an issue along with all of the other requirements that are placed upon appraisers. If we could get to a point at some time in the future, a point of stasis where there aren't as many changes going on, it would make it—

Mr. PEARCE. All right. I get it. I get the point. I am running out of time.

So, Mr. Garber, Mr. Park said that 25 years is not hardly, just barely a glimmer in a matter of a bureaucracy. I am kind of paraphrasing it. When I look at Uber, it didn't exist 5 years ago, and now it is worth about $67 billion. So markets are really generating fast. This idea that we can't get a coherent way of regulating in 25 years, is that something you agree with or disagree with?

Mr. GARBER. I think there is clearly a better model that Congress has recognized recently, and that is the nationwide mortgage licensing system to the States.

Mr. PEARCE. All right. Thanks. I appreciate it.

I yield back, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman yields back.

With that, we have the gentleman from Texas who has a second question. He is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman.

Ms. Wagner, you had something that you were trying to complete. Would you want to do so now?

Ms. WAGNER. Thank you, sir.

I just wanted to point out that I think that there are some really important market forces at work, and maybe when I said a handful of appraisers I was discussing in West Virginia there are some identifiable bad actors. But I think that the market forces at work really created a situation where the lending industry was able to put substantial pressure on appraisers that compromise their independence and compromise their ability to provide adequate values.

And so, with the requirement of appraisal independence in Dodd-Frank, I think that that really helps to ensure that there is some independence there and that those market forces don't interact in order to put pressure on people to increase values or change values.

And in addition, I think that the uniform standards of professional appraisal practice help create standards that appraisers can be reviewed according to and can ensure that there are adequate protections in place for both consumers and homeowners and the economy as a whole. So I think that both of those systems are very essential.

Mr. GREEN. Thank you. I do agree with what you have said. I would add this. We do agree, I believe, that from time to time even the best of us can make mistakes. And much of what we do is based upon not only some standard, but also some evaluation that is subjective. And when those mistakes are made, we would want to have a process by which they can be corrected.

I was a judge for 26 years. I thank God that there was an appeals process. Over the 26 years I was not perfect. I was better than everybody else however.

So the point is that we do need to have a methodology by which we can achieve the balance, and that is what I would like to work with you on.

Ms. Wagner, I really like your input, and I like yours, too, Mr. Brady, because I think between the two of you we can strike that balance.

Now, let me go over to Mr. Park.

Mr. Park, just to get some understanding, first let me start with this basic premise. Do you agree that most people who commit fraudulent acts that they don't expose themselves, that they pretty much decide that this is something they will keep to themselves or they will keep it within a certain circle of people?

And I mention this because there seems to be the belief that you have the responsibility of eliminating fraud and that you are some sort of cop on the beat. I don't think that is your function. Am I correct?

Mr. PARK. No. I think that the Appraisal Subcommittee should have a role in preventing fraud whenever it can and has the authority to do so. But that authority largely resides within the States in terms of dealing with the individual transactions where fraud might occur.

Mr. GREEN. And my point is, however, that if it comes to your attention, if you have the opportunity, you would act. Is that a fair statement?

Mr. PARK. We would act within the confines of the law, absolutely. And we have tracked fraudulent—reports of appraisal fraud in the States so that we can work with the States when that becomes a real problem, again, through a partnership, not from the perspective of the Federal Government telling the States how they should handle their problems with fraud.

Mr. GREEN. So you are not the supervisor, you work with, you don't dictate to.

Mr. PARK. It depends on the issue. But when we do have the authority—

Mr. GREEN. Well, let's just talk about generally speaking.

Mr. PARK. —we do act in a supervisory role.

Mr. GREEN. Mr. Park, excuse me. Let's talk generally speaking, if we may. Generally speaking, do you supervise the activities of the States?

Mr. PARK. Yes.

Mr. GREEN. And when you supervise the activities of the States are you responsible for ascertaining whether or not fraud exists?

Mr. PARK. We are not directly responsible for that, no, sir.

Mr. GREEN. Okay. That is the point that I have been trying to help you make, Mr. Park. You are not the guy who acquires the empirical evidence to move forward. Is that a fair statement?

Mr. PARK. That is correct.

Mr. GREEN. That is the point, Mr. Park. There are people who seem to be attributing this to you.

Mr. PARK. Point well made.

Mr. GREEN. Thank you, Mr. Park.

I am going to yield back, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman yields back.

With that, we will go to another gentleman from Missouri. You guys are being inundated with us today. Mr. Clay is recognized for 5 minutes.

Mr. CLAY. Thank you, Mr. Chairman.

And I wanted to ask the panel, according to an educator at the Appraiser Institute, the average age of an appraiser is 55 years of age and the main barrier for entry into the profession is the requirement of employment. The employment requirement is an appraiser trainee has to work under a certified appraiser for 2,500 hours and a minimum of 2 years. So even if a person completes the educational process successfully, they still face a barrier of finding employment to complete the on-the-job training requirement.

My question to the panel is, how can we create an environment to help appraiser trainees to complete the employment requirements to become a certified appraiser? And I guess I will just start with Mr. Park and go down the line.

Mr. PARK. It is important that the appraisal regulatory system continues to look at new ways to bring people into the profession. There has been a lot of progress made in terms of the requirements for appraisers to enter the profession in terms of increasing those requirements.

. Mr. Bunton can speak to this also since it is the Appraiser Qualifications Board that is setting these requirements. But they have established a national uniform licensing exam, they have increased education requirements. And now they are looking at reducing the experience requirements, which historically have been a significant barrier to entry, because it is difficult to find a supervisor to train you as a trainee to get the necessary hours for your credential.

Mr. CLAY. Thank you.

Mr. Bunton.

Mr. BUNTON. Yes. The problem we have generally is also users of appraisal services do not want to engage trainees. So if I own an appraisal firm, I don't want to have trainees because they are really not much value to me.

As far as the experience requirement, 2,000 hours you mentioned, that is sort of a last vestige from an apprenticeship-type operation. We are moving to a profession. And our board is looking at case study courses and also an exam where you could test out essentially of a lot of that time and you become more valuable to an appraiser as a trainee much quicker than the 2,000 hours over 12 months.

Mr. CLAY. And, Mr. Bunton, I guess one of my concerns is that it brings, it adds an extra burden when you try to strive for diversity in this profession. Being a former realtor, we rely on appraisers quite a bit. So I was wondering, has that issue arisen in your industry and has anyone tried to address it?

Mr. BUNTON. We have. On several occasions we actually solicit. We have four boards that we have to populate every year, and we solicit it. We solicit minority groups, we solicit all types of people to get as many qualified applicants as we can get in there.

Mr. CLAY. Thank you.

Ms. Trice, anything to add?

Ms. TRICE. The only thing to add, I think it is a couple of problems. We have set the bar too high. The number of hours required to work with a mentor, you can actually become an airline pilot and have less experience, but you are responsible for several hundred souls, and nobody has ever died in the appraisal process to the best of my knowledge.

But the other problem is really an economic one, and we have had a compression of fees. And it is a very complicated topic, but we have a component of Dodd-Frank on customary and reasonable fees that has never been enforced. And so we have increased the requirements for appraisals, but they make about half of what they used to make. So nobody is going to want to enter the profession with that kind of economic environment.

Mr. CLAY. I see.

Mr. Garber has the institute done anything to try to make the workforce—

Mr. GARBER. Yes, absolutely we have. It is punitive right now to take on a trainee, very difficult process. We have a lot of—there are rules, regulations have been built up around that process. We do need simplification of that. Those could be modified significantly.

We have offered, and we don't agree with The Appraisal Foundation on everything obviously, but an area that we have been talking with them very closely is on the development of an experience alternative or to earn experience in a classroom situation in a tested environment. So to actually enable, where you can't find a mentor-mentee relationship, to actually earn that experience in a classroom under a tested situation.

Mr. CLAY. Can they complete?

Chairman LUETKEMEYER. Yes.

Mr. BRADY. I would just add, training is important. I don't know the number of hours and I am not in the professional business of appraisals, but where you go to the AMCs and you have a pool of appraisers, it doesn't mean that their expertise is new construction or existing. And so we have to maybe look at that more in detail as to if I have a new construction product I get in the pool, they have never done a new construction. So training and continuing education on this process is very important.

Mr. CLAY. Thank you.

Ms. Wagner, anything to add?

Ms. WAGNER. Just briefly. I think from talking to appraisers in my State, I think that having some compensation for supervisors would be helpful because I think it is very costly for people to bring on new trainees and that they are not getting adequately compensated for that.

Mr. CLAY. I see.

Thank you all very much for your responses.

Mr. Chairman, my time it is up.

Mr. PARK. Could I make one comment to that?

Chairman LUETKEMEYER. Sure. Go ahead, briefly.

Mr. PARK. One of the issues that we are grappling with right now is trying to educate lenders on the ability for lenders to use trainees in their transactions.

Historically, trainees have served as that force multiplier for appraisers. Once you get a trainee trained to a certain level where they can do the inspections and they can do some of the analysis and data gathering without that supervisor being involved every step of the way, it makes it much more economically viable to bring on trainees. Right now there are requirements that are outside of the Federal Government that limit the ability of trainees to be able to participate.

Mr. CLAY. Thank you.

Chairman LUETKEMEYER. Thank you.

With that, I have a couple of follow-ups, and then we will wrap up here.

Mr. Garber, in your testimony you argue in favor of limiting the activities of The Appraisal Foundation to prevent potential conflicts of interest. Can you explain what those conflicts of interest are?

Mr. GARBER. Sure. Thanks for the question.

Whenever you have a statute that recognizes an entity, obviously, there is great responsibility that is given to that organization, but then there is also a great privilege that comes with it. So if you get special standing and recognition, they are given recognition and powers, the public looks at them in a certain respect as an authority in certain areas. And it is very common to address that for Congress to set forth limitations in particular areas. The limitations are important because it helps level the playing field. It doesn't give one organization an advantage over another.

That is where we have been expressing concern relative to the move to create a third board under The Appraisal Foundation, the Appraisal Practices Board. That is a board that was directed by the Appraisal Subcommittee for the foundation to undertake to develop rules around methodologies. At the same time, the foundation was setting up an education arm to offer education around those entities or those valuation advisories.

We were concerned that that was essentially setting up a situation where there is too much centralized authority. If you have centralized authority in the area, the full range of valuation, including standards, qualifications and the methodologies, there is just a very strong potential for conflicts of interest to exist on education and on credentialing.

And Congress has recognized that, as I said. In the SAFE Act, under the Nationwide Mortgage Licensing System, there is a very strict prohibition for the Conference of State Bank Supervisors to not get involved in education activities. The same thing under the National Association of Registered Agents and Brokers. NARAB has a very similar provision. Because, again, it is a nonprofit organization, it is supposed to be a neutral, it is given special standing in the industry to be a neutral body within that universe. But it comes with responsibilities and privileges, and we ought not set up a situation where we are tilting the scales and giving an advantage to one group or to the other.

Chairman LUETKEMEYER. Mr. Park, do you want to?

Mr. PARK. If I may correct the record. That is the second time Mr. Garber indicated that the subcommittee directed The Appraisal Foundation to establish the Appraisal Practices Board. That is not the case.

There was a meeting, this predated my time at the subcommittee, but there was a meeting of the subcommittee where there was a discussion regarding the need for appraisers to have additional education regarding—at that time the hot button was declining markets and the Federal regulatory agencies were seeing problems with appraisers' ability to handle appraisals in declining markets.

The subcommittee never in any way directed The Appraisal Foundation to establish the Appraisal Practices Board.

Chairman LUETKEMEYER. Mr. Bunton, I am sure you have a comment.

Mr. BUNTON. Thank you. I would just like to address the conflict of interest issue. I think their testimony references a course approval program which we put in place primarily at their behest. They also mentioned we shouldn't be in education. They developed courses for us and donated them to us.

And as far as the Appraisal Practices Board, most appraisers do not belong to a professional society, and that board issues voluntary guidance, free of charge, no Federal funds. The story behind the story here is that in 2010 they were faced with suspension from the foundation for conduct. They resigned rather than face suspension. So now, while they were once an advocate, they have become an adversary, unlike the other 95 organizations affiliated with us.

Mr. GARBER. If I could?

Chairman LUETKEMEYER. Okay. No, we are going to move on.

Mr. Park, we want to clarify what you have been saying with regards to the registry. Apparently one of your statements said that you had the ability to take people off, and now you are saying the States are the one that really put people on or off. What is your final statement here?

Mr. PARK. Under certain conditions the Appraisal Subcommittee does have the ability to remove an appraiser from the national registry.

Chairman LUETKEMEYER. Okay, what you are saying is under Dodd-Frank you do have the authority to take them off?

Mr. PARK. Dodd-Frank gave us additional authority to remove appraisers and appraisal management companies from the national registry for up to 90 days in lieu of State action.

Chairman LUETKEMEYER. Okay.

Mr. PARK. So if a State was simply refusing to take action against an AMC or an appraiser who had demonstrable issues, then the subcommittee could take such an action.

Chairman LUETKEMEYER. Okay. So what you are saying is normally the State takes care of all this, but you are the remover of last resort, so to speak?

Mr. PARK. That is correct.

Chairman LUETKEMEYER. All right. Very good. Thank you.

That ends my questions. I do have some comments here.

I appreciate everybody's time today. You guys have been great. It has been a very spirited discussion. And I think it shows that we certainly have some issues here.

You know, 2008 showed that there were some problems in the appraisal industry. Dodd-Frank was an attempt to fix it. Like any bill, it is well intentioned. I am sure there are some tweaks that need to be done. Some good things that came out of it and probably not some good things. And so we want to work with you to find solutions to those things that don't work, to make sure that we fix them. We have had everything from blow the system up to just tweak it a little bit. So it has made for an interesting discussion today.

At the end of the day, the appraisers need to maintain their independence, but they need some flexibility. Ms. Wagner made a comment a while ago that flexibility is bad and it leads to fraud, which impugned the integrity of every appraiser out there, which I thought was remarkable. It was breathtaking, actually.

But I think that generally the appraisers are caught in a bind from the standpoint that what you do is give a snapshot in time of what the value of that property is today. Tomorrow that property will have a different value, it could go up, it could go down.

I have a daughter who lives in Denver, Colorado. All of you know Denver is a market where the real estate just keeps going up and up and up. She built a new house 3 years ago and can probably have close to 40 percent, if not 50 percent increase in value in that amount of time. Now, its value, the price of construction hasn't gone up, but the value of the home has gone up.

I live in rural Missouri. I can tell you, we have a real problem with appraisers. We have no appraisers in my county, period. We have a county of 25,000 to 30,000 people and no appraisers, zero, in my county. They are gone.

I said a while ago I have a friend who is in the business and it is very difficult, as you have talked about, to get past the certification problem.

So it tells me we have some difficulties and that the bottom line is we have to have appraisers to make sure that there is a trust in the value of the property and the people who buy it and finance it can believe in the value of that property for that day.

And so we want to work with you and we want to continue to have this discussion, and we certainly appreciate all of you being here today and having this, I think, very spirited and very informational discussion. Thank you.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, this hearing is adjourned.

[Whereupon, at 11:55 a.m., the hearing was adjourned.]

A P P E N D I X

November 16, 2016

National Association
of Home Builders

Testimony of Ed Brady

On Behalf of the
National Association of Home Builders

Before the

United States House of Representatives
Subcommittee on Housing & Insurance of the
Committee on Financial Services

Hearing on

"Modernizing Appraisals: A Regulatory Review and the
Future of the Industry"

November 16, 2016

Chairman Luetkemeyer, Ranking Member Cleaver, and members of the Subcommittee, I am pleased to appear before you today on behalf of the National Association of Home Builders (NAHB) to share our views on the regulatory structure of the appraisal industry and suggestions for ensuring an efficient and effective appraisal industry. My name is Ed Brady, and I am a home builder and developer from Bloomington, Illinois and NAHB's 2016 Chairman of the Board.

NAHB represents over 140,000 members who are involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. NAHB's members construct approximately 80 percent of all new housing in America each year, and help provide decent, safe, and affordable single family and multifamily housing to many of our fellow citizens.

NAHB believes that accurate appraisals are essential to a healthy and sustainable housing finance system. Yet, appraisals remain a challenge for the housing industry. Members of NAHB continue to identify impediments that hamper appraisers' ability to provide accurate valuations of residential real estate. The current appraisal system is impaired due to inconsistent and conflicting standards and guidance; inadequate and uneven oversight and enforcement; a shortage of qualified and experienced appraisers; and, the absence of a robust and standardized data system. NAHB believes these problems must be addressed in order to restore confidence in the real estate market and to establish a foundation for sustainable growth of the US economy. This can only be accomplished through sound valuation practices, policy, and procedures that produce more credible valuations under all economic circumstances.

NAHB appreciates the Subcommittee's focus on issues impacting the appraisal industry, including effectiveness of the current regulatory structure, provisions of the *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* that pertain to appraisals, and the role of appraisals in a 21st century marketplace.

NAHB is a strong proponent of a sound and effective appraisal industry. NAHB has been a leading advocate for improving the valuation process and has undertaken a number of actions to raise awareness and address the adverse impacts from inaccurate appraisals on the housing sector. This testimony reviews challenges and recommended solutions that NAHB has identified and developed through our experience working with appraisal and financial industry stakeholders and feedback from NAHB members.

NAHB Activities

NAHB has been significantly engaged on this issue since the financial crisis. NAHB conducted five Appraisal Summits to provide opportunities for the agencies and organizations that establish appraisal standards and guidelines to join housing stakeholders in a constructive dialogue on major appraisal topics of concern. The goal of the Appraisal Summits was to bring all the interested parties together to identify recommendations and solutions that participants could jointly pursue to improve the appraisal process. In addition, NAHB formed an Appraisal Working Group, consisting of home builders and representatives from the financial and appraisal sectors, to analyze the appraisal process and develop recommendations for improvement.

As a result of these efforts, NAHB developed a "Comprehensive Blueprint for Appraisal Reform" which outlines recommendations for improving the appraisal system by streamlining regulations and devoting adequate resources to ensure effective oversight and enforcement.

NAHB believes that having accurate, timely and more robust data (including data on new construction) is essential to ensuring accurate valuations and has been working with many stakeholders to be sure information is available and can be shared. NAHB continues to pursue opportunities to ensure that new construction data is available to appraisers in order for accurate valuation of new homes.

NAHB also has been encouraging banking and housing regulators to establish workable procedures for expedited appeals of inaccurate or faulty appraisals.

NAHB has also been a long-standing member of The Appraisal Foundation's Advisory Council and has provided input to The Appraisal Foundation on valuation advisories and other documents that it has released for public comment.

Overview

The housing recovery has been impeded by ongoing problems in the U.S. residential appraisal system. While lenders, federal banking regulators and federally related housing agencies implemented corrective measures in response to valuation breakdowns that came to light in the wake of the Great Recession, and Congress mandated additional measures in the Dodd-Frank Act, these steps did not address fundamental flaws and shortcomings of the U.S. residential appraisal framework. Improper appraisal practices, a shortage of experienced appraisers and inadequate oversight of the appraisal system continue to restrict the flow of mortgage credit and retard the housing recovery. NAHB is not advocating that appraisals should be higher than the real market. Rather, our goal is to establish an appraisal system that produces accurate values through all phases of the housing cycle.

The principal focus of reforms to date has been on eliminating undue influence on appraisers to produce inflated valuations that facilitate transactions. However, when home prices began declining, improper appraisal practices exacerbated the slide in values. Some appraisers used distressed sales – many of which involved properties that were neglected and in poor physical condition – as comparables in assessing the value of brand new homes, without accounting for major differences in condition and quality. Without such adjustments, the two housing types are not comparable. The inappropriate manner in which distressed sales were utilized distorted home valuations. Use of the cost and income approaches in conjunction with the comparable sales approach could mitigate such distortions.

The dramatic increase in the use of Appraisal Management Companies (AMCs) is another factor contributing to inaccurate appraisals. Some AMCs have reduced appraiser compensation, which has led to more activity by appraisers with less training and experience, and shortened turnaround times for valuations to as little as 48 hours. These changes have had a significant adverse effect on appraisal quality.

Other challenges facing the appraisal industry include shortcomings in appraiser training and experience in dealing with new construction and green building. There is insufficient new construction, energy efficiency and green building data available to appraisers. Further, current valuation practices do not provide a process for expedited appeals of inaccurate or faulty appraisals. Oversight of appraiser qualifications and appraisal practices falls to the individual states, and many jurisdictions have inadequate resources to adequately perform this function. In some states, fees collected for appraiser licensing and certification are swept into a general fund and are not utilized in appraisal/appraiser oversight and enforcement.

Current Challenges and Recommendations

Federal and State Oversight Is Complex and Flawed

Federal Regulatory Oversight

It has been more than 25 years since the establishment of the Appraisal Subcommittee (ASC) in August 1989, pursuant to Title XI of Financial Institutions Reform Recovery, and Enforcement Act (FIRREA) and the establishment of The Appraisal Foundation in 1987. The ASC is charged with overseeing the activities of the states and the Appraisal Foundation. The ASC reviews each state's compliance with Title XI of FIRREA and also monitors the requirements established by the Federal Financial Institutions Examination Council agencies regarding appraisal standards for federally-related transactions. All ASC operations, including oversight of the Appraisal Foundation, are funded by state certified or licensed appraisers, each of whom pays a $25 annual National Registry fee to the ASC as part of their state registration fee.

The Appraisal Foundation was created to implement the Uniform Standards of Professional Appraisal Practice (USPAP). The Appraisal Foundation is charged with oversight and administration of the Appraiser Qualifications Board (AQB), the Appraisal Standards Board (ASB) and the Appraisal Practices Board (APB). The AQB establishes the qualification criteria for state licensing, certification and recertification of appraisers. FIRREA mandates that all state certified appraisers must meet the minimum education, experience and examination requirements promulgated by the AQB. The AQB has also developed voluntary criteria for personal property appraisers. The ASB sets forth the rules for developing an appraisal and reporting its results. In addition, it promotes the use, understanding and enforcement of USPAP. FIRREA requires that real estate appraisals used in conjunction with federally-related transactions be performed in accordance with USPAP. USPAP contains the recognized standards of practice for real estate, personal property, and business appraisals. The APB, established in 2010, provides voluntary guidance on valuation methods and techniques.

The current residential appraisal system continues to face many challenges due to inconsistent and conflicting appraisal standards and guidance as well as inadequate oversight. NAHB believes that fundamental appraisal system reform must be a principal element of efforts to rebuild the nation's housing finance system. Coordination and accountability currently are lacking and there are major gaps in the system.

Supporting this view is the Government Accountability Office (GAO) report, *Real Estate Appraisals – Appraisal Subcommittee Needs to Improve Monitoring Procedures*[1]. The report to the Committee on Banking, Housing and Urban Affairs of the Senate and the Committee on

[1] Appraisal Subcommittee Needs to Improve Monitoring Procedures
GAO-12-147: Published: Jan 18, 2012.

Financial Services of the House of Representatives was a requirement of the Dodd-Frank Act. The purpose was to determine the ASC's ability to monitor and enforce state and federal certification requirements and standards. The failures in the process noted by GAO perpetuate inaccurate home valuations, negatively affect housing demand and are obstacles to the full recovery of the housing market.

Major reforms in appraisal practices and oversight are needed to ensure that appraisals accurately reflect true market values and do not contribute to price volatility. NAHB recommends that federal oversight of appraisal activities be strengthened through streamlining and coordinating the current regulatory framework to devote adequate resources and ensure effective oversight and enforcement.

State Regulatory Oversight

Oversight of appraiser qualifications and appraisal practices falls to the individual states, and many jurisdictions have inadequate resources to adequately perform this function. In some states, fees collected for appraiser licensing and certification are swept into a general fund and are not utilized in appraisal/appraiser oversight and enforcement.

In September 2013, NAHB partnered with the Association of Appraisal Regulatory Officials (AARO) to conduct a survey of individual state appraisal regulatory boards on a variety of topics intended to identify best practices for enforcing and administering real estate appraisal laws in member jurisdictions. Additionally NAHB reached out to a variety of key state regulators of different sizes and background to acquire additional insight. The following are best practices identified by these discussions and the survey.

Structure

Many State Appraisal Boards are responsible for the enforcement of a number of other professional services, which reduces their capacity for appraisal oversight and enforcement. Eighty percent of the states responding to the survey are responsible to oversee other professional activities. Strong state appraisal regulation requires:

- Independent and self-funded agency.
- Well-defined policy and automated processes.
- Umbrella agencies with well-defined boundaries and strict enforcement policies.

Dedicated Resources

A significant issue facing the State Appraisal Boards is inadequate resources. In many cases personnel are shared and funds are swept from appraisal activities into the state's general fund. Adequate appraisal resources require:

- Sufficient dedicated staff to carry out proper enforcement.
- Legal counsel dedicated to the appraisal program.
- No sweeping of appraisal-related funds into the state general fund.
- Independence from other state licensing agencies.

Governance

Effective governance is needed for successful disciplinary action. It is important that the board is fair, transparent and is representative of the real estate community. Members of the board must also have sufficient information and time to make an accurate decision. The governance framework should be:

- Well rounded board with members from:
  - Appraiser community (majority)
  - Lending community
  - Appraisal Management Company
  - Builder and Realtor community
  - Public members from the community
- Staggered terms for board members

Standardization

Standardization of state oversight practices within and across the states would provide numerous efficiencies and improve reciprocity between the states. This would involve:

- A forum for interaction that is utilized by all states.
- Best practices education for state appraisal agencies. Access to a national repository for shared background checks for appraisers.
- A repository of data to be shared by each participating state.
- Unique ID for appraisers and AMC's.
- Standardized reservation process for AMC's with a unique ID.
- A standardized complaint form.

Communication

The housing crisis highlighted the importance of clear and prescriptive communication between stakeholders. Accurate and timely communications will also provide all parties a common language as the housing finance and valuation communities work together to identify and implement housing finance reforms. An effective appraisal board communication system requires:

- Good communication with the federal ASC, including clear and timely interpretations of AQB requirements to assist states in preparation for the two-year state review process.
- Education for industry stakeholders on state appraisal regulatory processes.
- Clear information on disciplinary procedures and actions on the website.
- Regular participation in AARO events and other networking opportunities to engage with industry stakeholders.
- Utilization of available tools such as The Appraisal Foundation's Disciplinary matrix.

Inconsistent Standards

In response to criticism that lax appraisals contributed to the financial crisis, more restrictive appraisal policies have been implemented by lenders, federal banking regulators, the Federal Housing Administration (FHA), the Department of Veterans Affairs (VA), the United States Department of Agriculture (USDA), and Fannie Mae and Freddie Mac (the Enterprises). Oftentimes, this has created a myriad of appraisal guidelines that are complex and inconsistent, causing confusion and frustration.

Appraisal standards are not clear, best practices have not been well communicated, and enforcement is not occurring in a consistent manner. For all sectors that interact with appraisers – consumers, home builders, realtors, lenders, the Enterprises, mortgage insurers – appraisal quality and appraiser competence remain tremendous challenges.

Frequently individual agencies are implementing appraisal standards that do not allow appraisers the degree of discretion and judgement intended in USPAP. This has prompted industry participants to impose overlays that further impede the ability of appraisers to produce accurate valuations.

NAHB believes efforts should be made to standardize appraisal requirements throughout the housing finance system so all parties are operating under the same set of rules.

Inaccurate Appraisals for New Construction

NAHB members are still seeing inaccurate appraisals that contain flawed data or are missing key pieces of information that cause an incorrect value opinion. NAHB believes the objective of an efficient and accurate collateral valuation process is to not have high or low appraisals but an appraisal that accurately reflects the value of the property enabling lenders to correctly understand the collateral risk and ensure solid lending decisions.

Appraiser Experience and Training

There are shortcomings in appraiser training and experience in dealing with new construction and green building. Valuing new home construction in particular is a highly complex analysis. Appraisers performing this analysis should have knowledge of new construction requirements, the ability to review building plans, etc. Appraisers must have a higher level of expertise in order to accurately and fairly complete their analysis.

NAHB believes that one way to address this concern and improve the quality of valuations is to strengthen education, training and experience requirements for appraisers of new home construction, including the establishment of greater education, training and experience requirements for those who are assigned appraisals of new construction. This will ensure that lot values and building costs, including those for energy efficient, green building and other evolving new construction techniques and mortgage products, are fully considered in valuation of new home construction. NAHB also recommends that the qualifications for appraisers of new construction be incorporated into appraisal regulations and guidelines of the bank regulatory agencies, Fannie Mae, Freddie Mac, FHA, VA and USDA.

Inadequate Data

There is a need for more robust data for newly constructed homes. Currently, there is insufficient new construction, energy efficient and green building data available to appraisers. Most Multiple Listing Services (MLS) do not adequately reflect new construction and energy efficient features. This lack of current data is a major cause of inaccurate appraisals for these properties.

NAHB recommends that the quantity and quality of data for new construction be improved through the establishment of an appraisal data base system for new construction; standardization of loan level valuation data by Fannie Mae, Freddie Mac, FHA, VA and USDA in their Uniform Appraisal Dataset (UAD); and, expansion of the UAD to include new construction, energy efficient and green building data standards. Discussions are underway to improve the representation of new homes in MLS databases. NAHB recommends these activities proceed expeditiously.

Valuation of Green and High Performance Properties

In addition to the availability of data for new construction, there remains quite a bit of confusion about accounting for energy efficient and other "green" features in new and existing properties.

The Appraisal Foundation has taken steps to improve appraisers understanding of valuing green features. The APB has been developing Valuation Advisories to provide appraisers information on how to identify green features, how to determine their relevancy, how to effectively utilize research and analysis, and how to account for green features in the three approaches to value (sales comparison, cost and income). The documents are intended to be a key source of information for appraisers and reflect the current options for green programs.

While NAHB supports the APB's goals, NAHB has been concerned about the process for developing the advisories and for taking into consideration stakeholder feedback. For example, NAHB submitted substantive comments on the First Exposure Draft of APB's Valuation Advisory #7 "Valuation of Green and High-Performance Property: One- to Four-Unit Residential" including correcting web links and references to documents that are no longer in use. NAHB was disappointed that the APB did not include any of our suggestions in the final version of the Valuation Advisory.

When the APB released the First Exposure Draft of "Valuation of Green and High-Performance Property: Commercial, Multifamily and Institutional Properties," NAHB expressed serious concerns about the document. In response to NAHB and other stakeholders' comments, the APB is making changes to the document and will release a second exposure draft. NAHB appreciates the APB's willingness to improve their processes and take stakeholder concerns into consideration. NAHB will continue working with the APB on updating the documents and keeping these documents relevant for a market segment that is growing and constantly changing.

Establish a Workable Appraisal Appeals Process

In real estate transactions, it is not unusual to find differences of opinion over the market value of the subject property. Such discrepancies can stem from inconsistent determinations on comparable sales, questions on appraisal methodologies and different interpretations of factual information. Disagreements over home valuations can happen in any real estate market, but they are more frequent during periods of challenging and volatile markets. In declining markets, such as those experienced during the 2005-2012 financial downturn, the markets saw a confusing mix of short sales, foreclosures, and market transactions. Such developments, however, continue to present challenges for real estate appraisers.

Buyers and sellers, builders and real estate agents can be held hostage by the current inability to promptly address legitimate questions on a valuation. The result is that all parties to the real estate transaction can be harmed when it is impossible to expeditiously and fairly challenge appraisals for errors of omission or commission.

Presently, if a home builder or a seller, or their agent, is involved in a transaction where the appraisal contains flaws that affect the value opinion, the only recourse is to the lender. If the lender has any process to address appraisal complaints, it is typically slow. By the time a response is received, if a response is issued at all, the transaction has, in all likelihood, fallen apart.

NAHB believes it is extremely important to establish a timely appeals process that is fair, balanced and appropriate to allow all parties to the transaction to appeal appraisals that do not meet USPAP standards or are based on inaccurate data or assumptions.

At present, there is no industry regulation or guidance establishing a standardized dispute resolution process outside of the Department of Veterans Affairs (VA) Loan Guaranty Program. Further, there is no single authority to expeditiously resolve an appraisal conflict nor is there any consistency amongst lenders should they decide to evaluate complaints of an appraisal that potentially contains factual errors or other flaws affecting the value opinion.

The Dodd-Frank Act (DFA) contains language that ensures all who have an interest in a real estate transaction may question the appraisal. Section 1472 (c) under the Appraisal Independence Requirements states:

> "(c) EXCEPTIONS.—The requirements of subsection (b) shall not be construed as prohibiting a mortgage lender, mortgage broker, mortgage banker, real estate broker, appraisal management company, employee of an appraisal management company, consumer, or <u>any other person with an interest in a real estate transaction</u> from asking an appraiser to undertake 1 or more of the following: [emphasis added]
>
> (1) Consider additional, appropriate property information, including the consideration of additional comparable properties to make or support an appraisal.
> (2) Provide further detail, substantiation, or explanation for the appraiser's value conclusion.
> (3) Correct errors in the appraisal report."

The Dodd-Frank provisions are incorporated in the banking regulators' Interagency Appraisal and Evaluation Guidelines at Section V. Independence of the Appraisal and Evaluation Program which states:

> "Consistent with its policies and procedures, an institution also may request the appraiser or person who performs an evaluation to:
>
> - Consider additional information about the subject property or about comparable properties.
> - Provide additional supporting information about the basis for a valuation.
> - Correct factual errors in an appraisal."[2]

Importantly, the Guidelines only state that the institution (lender) can make this request, it does not use the Dodd-Frank language that would allow other parties to make this request to an appraiser, i.e. the first part of the Exceptions provision above.

Many lenders and AMCs refer to the process they have to enable such requests as a "Reconsideration of Value" or ROV. To avoid potential adverse influence on the appraisal, the typical policy is to require anyone with questions to submit those requests through the lender rather than going directly to the appraiser.

FHA permits an underwriter to request a clarification or ROV from the appraiser when the appraiser may not have considered all of the information that was relevant on the effective date of the appraisal. The underwriter must provide the appraiser with all relevant data that is necessary for a reconsideration of value.[3]

NAHB builder members report that the current lender and FHA ROV process is not working. Despite the language in Dodd-Frank, the ROV process does not allow <u>all</u> parties to a transaction to provide additional information directly to the appraiser. All contact with the appraiser must be initiated by the lender/underwriter who may or may not process the ROV request. Further, the ROV process cannot be started until after the appraisal is issued. In extremely active markets, such as currently, the appraisal may not be completed until shortly before the closing date which leaves little time for an ROV. As a result, builders often will cover a small difference between the sales price and appraisal or, for larger differences in the sales price and appraised value, will lose the sale.

Builders have reported some success with the VA's process mentioned above. The VA's <u>Tidewater Initiative</u>[4], introduced in 2003 allows all parties to the transaction to provide the appraiser with additional information prior to the formulation of the appraiser's initial value opinion, which the VA refers to a the Notice of Value (NOV). The policy is known as the Tidewater Initiative because it was initially tested in the Tidewater region of Virginia.

The purpose of the Tidewater Initiative is to encourage VA program participants to provide relevant market data to VA fee and staff appraisers during the appraisal process to assist the

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[2] 75 FR 237 (December 10, 2010) p. 77457.
[3] FHA Single Family Housing Policy Handbook 4000.1 Section II.A.3viii.
[4] VA Circular 26-03-11, "New Procedures for Improving Communications with Fee Appraisers and Streamlining Reconsiderations of Value" (December 22, 2003).

appraiser in identifying relevant information they may not have had access to that ultimately creates a more accurate value opinion. Prior to issuing a NOV, a VA appraiser is required to notify a designated point of contact (POC) if the appraised value will come in below the sales price of the subject property. The appraiser will not be at liberty to discuss the contents of the appraisal with the POC at this point beyond explaining that they are calling for whatever additional information the POC may be able to provide. Full cooperation is expected between the appraiser and the specified POC or lender. Once the POC or lender has been notified, they will have two working days to provide additional information to the fee appraiser in a specified format. After receipt of any additional information, the appraiser will proceed with their due diligence and complete the report, which may or may not be affected by the additional information.

NAHB recommends federal agency adoption of a standard appraisal appeals structure similar in design to that of the VA's Tidewater Initiative. This could be done through an amendment to Title 14 of the Dodd-Frank Act directing mortgage and banking regulators to develop and implement a standard appeals process.

Conclusion

Collateral valuation is a critical component of the mortgage decision. While there have been a number of positive changes to the appraisal system since the financial crisis, there remain a number of unresolved issues. Confidence in home values is essential to a housing market recovery as well as an important component to a robust primary and secondary mortgage market.

NAHB stands ready to work with appraisal, housing and financial stakeholders to address the real challenges we face in restoring the public trust in how we build, transfer, value and finance the American consumer's most valuable asset. We must work together to reform appraisal practices that support accurate and sustainable values. Solving these issues, in the short and long term, is a critical step toward establishing an efficient and sustainable housing finance market. In fact, it is vital to address appraisal standards, processes and oversight as Congress undertakes reform of the housing finance system.

NAHB appreciates this Subcommittee's attention to these issues. NAHB looks forward to working with the House Committee on Financial Services and others to identify and implement solutions to strengthen the process that measures the value of many Americans' most valuable asset – their home.

Testimony of
David S. Bunton, President
The Appraisal Foundation

Modernizing Appraisals: A Regulatory Review and the Future of the Industry

U.S. House of Representatives
Committee on Financial Services
Subcommittee on Housing and Insurance

November 16, 2016

THE APPRAISAL FOUNDATION
Authorized by Congress as the Source of Appraisal Standards and Appraiser Qualifications

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INTRODUCTION

Mr. Chairman and members of the Subcommittee, The Appraisal Foundation greatly appreciates the opportunity to appear before you today to offer our perspective on the regulation of real estate appraisers and the future of the profession.

There are many misconceptions about The Appraisal Foundation and let me begin by stating that the Foundation is not:

- a government agency or regulatory body;
- created by Congress;
- an appraisal trade association.

Rather, the Foundation:

- is a non-profit 501(c)(3) educational organization;
- was founded by eight national appraisal organizations 29 years ago;
- serves as an umbrella organization comprised of approximately 100 organizations and government agencies with an interest in valuation;
- was created to foster professionalism in appraising.

We provide private sector expertise in the real property appraiser regulatory system. The Foundation was given specific authority by Congress in 1989 (Title XI of FIRREA) regarding the real property appraiser regulatory system. The Foundation does not have any regulatory authority, but it provides tools for the regulatory community. Specifically:

- individuals seeking to become a trainee appraiser, supervisory appraiser, state licensed appraiser or state certified appraiser must meet the minimum qualification requirements established by the Foundation's Appraiser Qualifications Board (AQB);
- all states and territories must use licensing and certification examinations either issued or endorsed by the Foundation's AQB; and
- all state licensed and certified real estate appraisers must adhere to the *Uniform Standards of Professional Appraisal Practice* (standards of conduct) written by the Foundation's Appraisal Standards Board (ASB).

On behalf of The Foundation, as a fair, impartial, and objective resource on valuation-related issues, thank you for the opportunity to address the specific topics on which you are seeking our perspective.

SPECIFIC TOPICS OF DISCUSSION REQUESTED BY THE SUBCOMMITTEE

Appraiser Regulatory Structure

Background
In the 1980s, the United States (U.S.) financial sector experienced a period of distress that was focused on the nation's savings and loan (S&L) industry. By 1984, Congress was already hearing complaints about faulty and fraudulent appraisals that were deepening the severity of the S&L crisis. To address the thrift industry's problems, Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), which ushered in a number of industry reforms. The main S&L regulator (the Federal Home Loan Bank Board) was abolished, as was the bankrupt Federal Savings and Loan Insurance Corporation (FSLIC). In their place, Congress created the Office of Thrift Supervision (OTS) and placed thrift's insurance under the Federal Deposit Insurance Corporation (FDIC). In addition, the Resolution Trust Corporation (RTC) was established to resolve the remaining troubled S&Ls. The RTC closed over 700 S&Ls with assets of over $400 billion. Taxpayers were left with over $120 billion in losses and a shaken confidence in the U.S. financial system.

Title XI of FIRREA (Title XI) created the unique appraiser regulatory system we have in place today. The purpose of Title XI is:

> *"to provide that Federal financial and public policy interests in real estate related transactions will be protected by requiring that real estate appraisals utilized in connection with federally related transactions are performed in writing in accordance with uniform standards, by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision."*

To serve this purpose, Title XI authorized the uniform appraisal standards and minimum appraiser qualification criteria established by The Appraisal Foundation (Foundation), and authorized states to establish appraiser regulatory programs to ensure effective supervision of licensed and certified appraisers who are eligible to perform appraisals for federally related transactions (FRTs). The Appraisal Subcommittee (ASC), an independent executive branch federal government agency, was created by Title XI within the Federal Financial Institutions Examination Council (FFIEC) to provide oversight to the appraiser regulatory system. The Association of Appraiser Regulatory Officials (AARO), a non-profit organization, was formed in 1991 to facilitate communication between regulators and others involved with the appraisal profession.

The emerging system brought about stability and consistency where previously there was none. Prior to the creation of the Foundation and subsequent adoption of Title XI, anyone could declare him/herself a real property appraiser, the associations for appraisers each had their own individual set of rules about appraiser qualifications and standards of appraisal practice, and only a handful of states had chosen to regulate the occupation. The inconsistencies and uncertainties made a negative impact on the market and contributed to the financial crisis.

In the 25 years since the implementation of Title XI, the system has evolved and significant improvements have been made. Policy makers, lenders, consumers, and others relying on the services of a real property appraiser have greater assurance in the profession because:

- Appraisers now meet increased education requirements in specific valuation topics, gain experience under careful supervision, and successfully pass a robust, national examination;
- Appraisers now practice under a single set of uniform, ethical standards (i.e., the *Uniform Standards of Professional Appraisal Practice*, or USPAP), which have been tested in the courts and are looked upon globally as a gold standard;
- State regulatory bodies are established as envisioned with 76 percent deemed "good" or "excellent" in their compliance reviews;
- State boards embrace knowledge-based enforcement by having sent 783 state regulatory staff members to investigator training since 2009;
- State boards, comprised primarily of appraisers, are effectively policing the profession with more than 19,000 disciplinary actions reported to the National Registry in the ten-year period from January 1, 2006 through December 31, 2015; and
- The system operates in an open and transparent manner with the entities working together and engaging stakeholders and the public when emerging issues arise.

These strides illustrate the benefits of uniting the private sector with state and federal regulatory entities for a more streamlined and accessible regulatory system.

Since the enactment of Title XI of FIRREA in 1989, Congress has addressed other crises by creating similar regulatory structures to ensure a national threshold of competency:

- With the advent of the Arthur Andersen and Enron scandals in 2001, Congress created the private sector Public Company Accounting Oversight Board (PCAOB) to ensure that the auditors of public companies adhere to independent and transparent national standards.
- Following the 2008 housing crisis, Congress passed the SAFE Act, which mandates that mortgage originators are subject to background checks, a uniform

set of educational courses, and a comprehensive examination. This system is administered by the Conference of State Bank Supervisors' wholly owned subsidiary, the Nationwide Mortgage Licensing System and Registry (NMLS).

Suggestion for State-Based Alternative to Federal Regulatory Structure
Some have suggested that the federal arm of the appraiser regulatory system currently in place be replaced with a state-based structure. They point to regulation of other professionals involved in federally related mortgage transactions: real estate agents, bankers, and attorneys, among others, and pose the possibility for creating a similar oversight structure for appraisers. Examining this concept further, one finds:

1. The Appraiser Membership Organization Structure is Fractured
   Unlike professionals whose support structure includes a comprehensive national association to which most members belong, namely: the National Association of REALTORS, American Bankers Association, Mortgage Bankers Association and the American Bar Association, appraisers do *not* have a primary membership organization to create consistency across the profession. There are numerous appraiser associations, most of which specialize in niche markets. Among others of various sizes and interests, examples include:

   - **Commercial appraisal** - Appraisal Institute (AI), American Society of Appraisers (ASA), and Royal Institute of Chartered Surveyors (RICS)
   - **Residential appraisal** - National Association of REALTORS (NAR), National Association of Independent Fee Appraisers (NAIFA)
   - **Rural appraisals** - American Society of Farm Managers and Rural Appraisers (ASFMRA)
   - **Mass Appraisal/Assessment** - International Association of Assessing Officers (IAAO)
   - **Easement/Government Right of Way** - International Right of Way Association (IRWA)

   Adding to this complexity, it is a widely held belief that approximately 70 percent of state licensed and certified appraisers do not belong to a professional membership organization or adhere to ethical guidelines that professional association membership dictates.

   One strong national association, like those that exist for the other professions, would help to ensure consistency state by state. Without similar organization for appraiser professionals, a state-based appraiser regulatory structure would be hampered by competing interests of numerous membership bodies.

2. <u>The Number of Appraisers is Comparatively Small</u>
   There are approximately 80,000 licensed and certified appraisers in the United States. This compares to two million real estate agents, two million bank employees, and 400,000 American Bar Association members. The other professionals involved in mortgage lending transactions dwarf the number of appraisers and their membership organizations have significantly more political sway. It may be difficult for a state-based regulatory structure to ensure appraisal independence and consistent adoption of a common set of qualifications and standards given the imbalance.

Keeping a small yet effective federal footprint in the appraiser regulatory system is critical to overcoming these issues. Appraisers are the only independent voice in a real estate transaction. Payment for their service is not connected to the purchase price or successful closing. There are important public policy reasons to ensure appraisal independence and prevent undue influence in providing an opinion of real property value. The authority of the federal government levels the playing field for these appraiser "Davids" versus their "Goliaths." A federal presence helps to ensure appraiser quality and independence so that appraisals performed in conjunction with federally related transactions can be regarded as credible and worthy of public trust. This small federal footprint—currently the ASC—is important to ensure consistency across the country for consumers and the mortgage finance system.

Leveraging the Federal Footprint to Streamline Regulatory Compliance
Technology has drastically changed since the enactment of Title XI, allowing for the electronic transfer of critical data and information. Likewise, the geographic market area of many appraisers now reaches beyond individual state borders and certification in multiple jurisdictions is common.

With minimum appraiser qualification requirements set by the Foundation and adopted by all jurisdictions, appraiser state application materials are mostly duplicative state by state. This creates an unnecessary administrative burden for both state regulators and individual appraisers.

To ease regulatory burdens, the Foundation has started conversations with its advisory organizations, state regulators, and others to explore the development of a national portal for submission of appraiser licensing and certification application information. The portal would be accessible by each state jurisdiction and function similar to the NMLS for mortgage licensing. Congress recently expanded the authority of NMLS to allow it to service other professionals involved in mortgage lending. Expansion of that system for appraiser licensing and certification is worth exploring, and funding for the connection to state regulatory bodies could be provided by the ASC as part of its authority to offer grants to states. Leveraging the federal footprint in this manner would streamline the regulatory process, relieve administrative burdens, and help the states as well as the appraiser professionals relying on state services.

Effectiveness of the Appraisal Subcommittee

The federal entity in the appraiser regulatory system is the ASC. It is an oversight body primarily designed to:

- Monitor the states, the Foundation, and the federal banking regulators regarding Title XI related activities;
- Ensure appraisers who perform appraisals for federally related transactions meet the qualifications set by the AQB of the Foundation, complete appraisals in accordance with uniform standards, and are subject to effective supervision; and
- Provide grants to the Foundation and the states for Title XI activities.

The ASC has worked to carry out its Congressional charge in these areas, but as we envision the future of the appraiser regulatory system, minor adjustments would increase its effectiveness.

Monitoring

Since the enactment of Title XI, the focus of ASC monitoring has been administrative—ensuring proper regulations are in place and processes are completed timely. The 2015 ASC Annual Report indicated that it monitored the work of the Foundation by attending meetings and reviewing documents, that it monitored the ASC member agencies by noting they had adopted appraisal-related rules and policies, and that it monitored state regulatory programs by on-site visits to review documents and attend regulator meetings. These primarily administrative reviews found no issues of concern with the Foundation and ASC member agencies, and 42 of the 55 state jurisdiction regulatory programs are currently deemed as "Good" or "Excellent" following compliance reviews.

To increase the effectiveness of the ASC, the function of monitoring should evolve to more substantive issues in the following areas:

1. Consistency in Enforcement Among the States: The organizations that provide input and counsel to the Foundation report wide differences among states in the application of disciplinary measures for appraisers who violate USPAP. The ASC should use the information gained during compliance reviews to analyze states' enforcement decisions and provide an annual report about the outcomes.

2. Proper Application of USPAP to Violations Charged: The ASC review process is limited to verifying that states are resolving complaints within a one-year time frame set by ASC policy. To increase effectiveness, the ASC should review the states' complaint resolution decisions to ensure that they are properly and consistently determining an appraiser's adherence to USPAP when completing appraisals. The findings of these reviews should be shared with the states and other interested parties, and could become the basis for educational and informational programs to be developed if inconsistencies are revealed.

3. Analysis of Complaints Referred to Banking and Appraiser Regulators Via the Appraisal Complaint National Hotline: The enactment of the Dodd-Frank Act gave the ASC the authority to create a hotline to receive and refer complaints of non-compliance with appraiser independence and USPAP. It also gave the ASC the authority to follow-up on complaint referrals to the states, financial institution regulators, and others to determine the status of the resolution. While an information and referral portal was established, the ASC should complete its charge by following up on referrals and publishing information about the resolutions.

To increase effectiveness while keeping the federal footprint small, the ASC should move to reviewing reports and information, instead of the labor-intensive and costly site and meeting visits, for those entities found to be compliant or without major concern in previous years.

A structural change would further help the ASC meet its monitoring requirements. The ASC is comprised of representatives of the Federal Reserve, Office of the Comptroller of the Currency (OCC), Federal Housing Finance Agency (FHFA), Federal Deposit Insurance Corporation (FDIC), Consumer Financial Protection Bureau (CFPB), National Credit Union Administration (NCUA), and the U.S. Department of Housing and Urban Development (HUD). The ASC staff is put in a difficult position by the mandate that they must monitor the agencies' appraisal-related activities from which their board members are appointed. This became evident with some of the agencies' rulemaking decisions to reduce the impact of Title XI by creating a myriad of exemptions to the definition of "federally related transactions" and increasing the threshold amount under which an appraisal is not required. This structure also impacted decisions made by the ASC about the Appraisal Complaint National Hotline. A more independent reporting structure would enable the ASC to more effectively carry out its Congressional mandates to monitor the actions of these agencies.

Ensuring Appraisers are Qualified

To ensure that qualified appraisers are qualified to develop appraisals used in conjunction with federally related transactions, the ASC maintains a National

Registry of state licensed and certified appraisers. The National Registry contains the names and credential information of individuals that the states have deemed to have met qualification criteria established by the AQB and whose practice has not been found in violation of USPAP. We are encouraged that the ASC is working to improve the National Registry by creating a unique identification numbering system that will identify appraisers individually rather than by credentials held as many appraisers hold credentials in multiple jurisdictions. To make the National Registry more robust, the ASC should capture additional information about the appraiser including primary area of appraisal practice (e.g., commercial, residential, litigation, assessment, etc.), primary location of practice territory (e.g., urban, rural), any professional designations held, and contact information (including email address). This information would help individuals select an appraisal professional who meets their needs and to communicate to all appraisers about items of importance.

Grants in Support of Title XI Activities

While no federal tax money is used to support the appraiser regulatory system, states are required to annually collect and submit to the ASC $40 per state licensed and certified appraiser. These funds support the work of the ASC, provide it with funding to issue grants to the Foundation to support Title XI-related activities undertaken by the Appraisal Standards and Appraiser Qualifications boards, and enable the ASC to provide grants to states to support Title XI activities in the areas of complaint resolution and data submission. In the last five years, these grants combined have ranged from 25 percent of the ASC's annual budget ($1.1M of its $4.27M budget in 2011) to less than 15 percent of its annual budget ($569,000 of its $3.8M budget in 2015). Without consistency in funding, the Foundation must seek alternative revenue sources and the states must increase licensing and certification fees for appraisers to fund state regulatory programs. Greater stability and equity in funding amounts would be helpful for planning and execution of Title XI by the Foundation and the states.

Establishing a funding distribution model would bring greater consistency and stability to support Title XI activities. As examples, the model could:

- Set a minimum percentage of ASC funds collected to be used for grants to the Foundation to fund Title XI-related activities (e.g., 25 percent);
- Set a minimum percentage of ASC funds collected to be used for grants to states to fund Title XI-related activities (e.g., 25 percent); and/or
- Set a maximum percentage of ASC funds collected that it may keep for its federal oversight responsibilities (e.g., 50 percent).

The Impact of the Dodd-Frank Act on the Current Regulatory System, Stakeholders, and Consumers

While the Dodd-Frank Act ushered in some beneficial regulatory reform, it also created its share of unintended consequences. Promoting appraisal independence is an admirable goal, but building upon the Appraisal Management Company (AMC) model first made prevalent in the *Home Valuation Code of Conduct* (HVCC) had its drawbacks as well.

The Good

Codifying specific appraisal independence violations in federal statute was a big victory for appraisers. With the passage of Dodd-Frank, loan originators, processors, underwriters, mortgage brokers, and real estate salespeople were put on notice that appraisers could not be "bullied" into making deals work. Dodd-Frank provided a laundry list of acts that would constitute violations of appraisal independence. While many involved in the residential real estate marketplace needed no such compelling legislation, appraisers stood up and took notice that provisions to safeguard their independence were now part of federal legislation. Dodd-Frank also included provisions that permitted appropriate communication with appraisers for legitimate business needs.

Dodd-Frank also included some consumer protection provisions aimed at predatory lending practices. Such practices significantly contributed to the real estate "bubble," which ultimately resulted in the loss of significant wealth to a great number of Americans.

The introduction of federal legislation that enabled the ASC to regulate AMCs was another positive aspect of Dodd-Frank. Many states implemented AMC regulation prior to the enactment of the federal law, but Dodd-Frank gave formal authority to the state appraiser regulatory agencies to do so. The federal regulations for AMCs promulgated by the ASC take effect in August 2018.

Dodd-Frank also authorized the Foundation's AQB to establish minimum requirements for trainee, supervisory appraisers, and licensed residential appraisers. Although prior to Dodd-Frank many states had voluntarily implemented the minimum qualifications for these classifications that were set by the AQB, the federal law assisted in greater consistency.

The prohibition against using Broker Price Opinions (BPOs) as the primary basis for evaluating collateral was also seen as a positive aspect of Dodd-Frank. While BPOs provide a valuable service in buying and selling real estate, they do not offer the independent, impartial, and objective analysis that an appraisal offers. Nor do they provide the depth and breadth of the analyses found in appraisals.

The Bad
Despite the specific exceptions noted in Dodd-Frank, many in the residential mortgage lending arena mistakenly equated the appraisal independence provisions with an appraiser being "radioactive." Such misunderstanding was relatively commonplace, but has been tempered more recently due in part to efforts of the Foundation, including the development of promotional material identifying these issues as "Common Myths" (Attachment 1) and elaborating on them at conferences and speaking engagements.

Dodd-Frank also reinforced the AMC appraisal procurement and management model to the point that many lenders mistakenly believed Dodd-Frank *required* them to use an AMC. Nevertheless, many lenders welcomed codification of the AMC model because it allowed them to outsource engaging appraisers, manage their progress for the duration of an assignment, and rely on them to perform at least a cursory review of the appraisal report. In addition, some lenders found the AMC model to be a newly discovered source of revenue. These lenders determined they could charge borrowers the "going rate" for appraisals, yet they weren't required to pay the AMCs since the AMCs receive the bulk of their funding from the appraiser. This resulted in many appraisers feeling like they were servants to a new master, and to add insult to injury, lost 40 to 60 percent of their appraisal fees.

Dodd-Frank benefited consumers by requiring lenders to provide a copy of the appraisal that was utilized in underwriting a loan. The CFPB went a step further and required lenders to provide borrowers with copies of *all* valuation products that were considered in conjunction with the loan application. Unfortunately, many borrowers were simply confused when receiving this information prior to closing. Some wondered why certain products reflected one opinion of value, while a different product showed another. And how was the appraisal fee the borrower paid actually applied to these various products? In an effort to aid in understanding, the Foundation created material that could be provided to borrowers upon receiving these valuation products (Attachment 2); unfortunately, the CFPB opted not to require lenders to provide it.

Dodd-Frank included a provision whereby the appraisal fee paid listed on the Closing Disclosure statement *may* delineate between the fee the appraiser received and the fee retained by the AMC. Unfortunately, the CFPB opted <u>not</u> to require the Closing Disclosure statement to separately identify these fees. This lack of transparency is a disservice to all parties, leading borrowers to believe the appraiser received the full fee paid when in fact it is generally about half of what is paid.

Dodd-Frank included provisions for appraisers to be paid customary and reasonable fees. Unfortunately, to date such provisions have not been consistently enforced. Further, many appraisers perceived such a provision to be incredibly ironic since the legislation further entrenched the AMC model where appraisers now received a fraction of the fees they had in the past.

The *De Minimis* Threshold and Federally Related Transactions

Background

In the summer of 1990, the federal financial regulatory agencies developed their appraisal regulations, which included a $50,000 *de minimis* threshold, with the exception of the Federal Reserve Board (FRB), which set its threshold at $100,000. Real estate transactions below this threshold would not have to be appraised by a state licensed or certified appraiser.

In the spring of 1992, the FDIC, the OCC, and the OTS revised the regulations and changed their thresholds for requiring a state licensed or certified appraiser to $100,000. In June of 1994, the federal financial regulatory agencies then increased the *de minimis* to $250,000, where it remains today. As a result of outreach meetings over the past year associated with The Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), there have been several recommendations that the current threshold of $250,000 be doubled to $500,000.

We strongly oppose such an increase because it would significantly dilute the intent of Title XI of FIRREA. Title XI was put in place to ensure the safety and soundness of our deposit insurance fund. The value of the underlying collateral in a lending transaction needs to be determined by a professionally trained appraiser who adheres to performance standards and is credentialed by a state. With the current median existing home sales price of $234,200, a $500,000 *de minimis* would exempt most residential mortgage transactions. An individual's primary residence is often their single largest investment and neither lenders nor borrowers would be afforded the protection of having a trained professional determine whether an appropriate price is being paid for a property.

Federally Related Transactions

Related to the *de minimis* is the issue of what constitutes a federally related transaction. When Congress passed FIRREA, the intent was that most residential mortgage transactions would be considered federally related transactions.

In the early 1990s, the federal financial regulatory agencies adopted a series of regulations that resulted in 12 instances where a transaction is no longer considered a federally related transaction (Attachment 3). These exemptions greatly reduced the number of federally related transactions. It is estimated that fewer than 20 percent of residential mortgage transactions are federally related transactions.

There continues to be a great deal of confusion in the marketplace about what constitutes a federally related transaction. Most individuals involved in the appraiser regulatory system are under the false impression that the majority of residential mortgage transactions are federally related.

For example, in August 2015 the AARO wrote a letter to the ASC requesting a definition of what constitutes a federally related transaction. To date, AARO has not received a response to their letter.

By raising the *de minimis* and very narrowly defining what constitutes a federally related transaction, the intent of Title XI of FIRREA has been significantly undercut.

A Shortage of Appraisers

In recent months there have been numerous reports of appraiser shortages, long waits to obtain an appraisal, and higher appraisal fees. The chart included with this testimony (Attachment 4)—developed by the ASC staff—illustrates the rise and fall of appraiser credentials as well as the correlation between appraiser credentials and mortgage originations. While this chart suggests that the shortage is not a national problem, there is no question that there are shortages being reported in certain markets.

Ironically, the number of state certified real estate appraiser credentials is almost ten percent higher today than it was ten years ago. However, there are several factors that may be causing localized appraiser shortages. In large part, these factors apply almost exclusively to the residential mortgage lending sector of the profession for the following reasons:

The Demise of the State Licensed Residential Real Estate Appraiser
As a result of the real estate crisis, Congress passed the *Housing and Economic Recovery Act of 2008 (HERA),* which required that appraisers for Federal Housing Administration (FHA)-insured mortgages must be "certified" by the state in which the property to be appraised is located or by a nationally recognized professional appraisal organization. Effective October 1, 2009, FHA no longer accepted new applications from state licensed residential appraisers per the HERA requirement. All roster appraisers must now be state certified and appear on the ASC's National Registry in order to conduct appraisals for FHA-insured mortgages.

This has had a very significant impact on the number of state licensed real estate appraisers. While some obtained the state certified real estate appraiser credential, many left the profession. A ten-year comparison of appraiser credentials (below) shows a decrease in the number of state licensed residential real estate appraisers by over 70 percent.

Active Appraiser Credentials

	2006	2016
Certified General	34,812	39,011
Certified Residential	46,701	49,550
Licensed Residential	29,921	7,950

The Education of Users of Appraisal Services

Another significant change that has occurred in recent years is the fact that many lenders today do not want licensed residential or trainee appraisers involved in the performance of residential appraisals. This decision occurred in large part because of the abundance of caution that lenders exercised following the economic crisis of 2008. The Foundation was surprised to learn that many lenders believe that Dodd-Frank prohibits them from using these individuals, which is simply not the case. Using state licensed residential appraisers and trainees would greatly reduce any backlog of appraisal assignments. Licensed residential appraisers are legally able to perform appraisals on the vast majority of residential real estate in this country (non-complex residential property with a loan amount below $1,000,000, and complex residential property with a loan amount below $250,000). In addition, trainee appraisers can perform appraisal assignments on any property a supervising certified appraiser is legally able to perform, provided the report is co-signed by that supervising certified appraiser. The Foundation is working with professional associations who represent lenders to raise awareness that the use of both licensed residential appraisers and trainee appraisers is permissible and should be encouraged.

The Economic Factor

Even with the "customary and reasonable fees" provision contained in Dodd-Frank (enacted in 2010), there is little debate that residential appraisal fees have stagnated in recent years. Whether it is due to the advent of AMCs or because some users of appraisal services view appraisals as a "commodity," there has been an impact on the number of appraisers who want to perform appraisals for residential mortgage lending. Many have opted out of residential appraising altogether or have diversified their practice to include such specialties as eminent domain, insurance, assessment appeal, and litigation support. While the number of residential appraisers remains strong, there may be a shortage of appraisers ***willing*** to accept assignments below a certain fee threshold.

A large number of residential appraisers believe the working conditions for many assignments in the residential mortgage lending sector are untenable. Many of the pricing and turnaround time models used by AMCs were developed for urban and suburban markets. In rural areas, many appraisers refuse to take on assignments due to: (1) the level of compensation; and (2) a short turnaround time requirement when the property is a considerable distance away. Some appraisers believe an AMC must "justify" the fee it is earning by placing greater scrutiny on appraisal reports, and create additional requirements for the appraiser.

Many clients and users of appraisal services have also asked for more in residential mortgage appraisal assignments. Performing an enhanced scope of work and providing more detail in a report should create an expectation of *higher* – not lower fees. Lower fees, quick turnaround time expectations, and increased client requirements result in an unsavory cocktail for many appraisers; from a strictly economic point of view, it is simply not worth their time.

The Dispersion Factor
While we can easily identify the number of appraisers in each state through the ASC's National Registry, how those appraisers are dispersed in their respective states is much more difficult to assess. There is little doubt that there are counties and towns around the United States that are underserved by appraisers; but that has historically been true to some degree. The Foundation believes that the significant reduction in the number of licensed appraisers has adversely impacted rural areas. Individuals who may have possessed multiple credentials in such fields as real estate sales, insurance, and real estate appraising may have let their licensed residential appraiser credentials lapse when the demand for their services dropped off significantly as a result of the FHA policy and refusal of lenders to engage them.

A Look Ahead
While the Mortgage Bankers of America projects a reduction of mortgage originations over the next two years, the Foundation has some concerns about the number of real estate appraisers 3-5 years from now and wants to ensure there are no unnecessary barriers to entry for qualified individuals seeking to enter the appraisal profession. It is for this reason the AQB is looking into alternative ways that individuals may meet certain qualification criteria requirements.

The Role of Appraisals in a 21st Century Marketplace

Appraisals performed by ethical and competent appraisers are a cornerstone of safety and soundness policies for financial institutions insured with federal funds. Without an independent, impartial, and objective opinion of value for collateral, lenders could make risky loans without the safeguard of knowing their investments are protected.

We have all witnessed financial crises that took their toll on financial and real estate markets and burdened U.S. taxpayers with a heavy debt. As discussed, the Savings & Loan Crisis of the 1980s brought about regulatory reform that included, for the first time, national requirements for the licensing and certification of real estate appraisers performing appraisals in federally related financial transactions.

Moving forward, what role will appraisals play? Although there are obviously fluctuations (e.g., "bubbles") from time to time, the long-term trend for real estate in this country is clearly one of appreciation. And the higher the property values, the larger the loans that homebuyers and homeowners will seek. Larger loans equate to potentially greater risk for financial institutions and the secondary market, thereby possibly creating increased exposure for the taxpayer. Therefore, it could be argued that in the years ahead, professional valuations will be even more important than they are today. However, appraisers will need to embrace new paradigms with respect to the roles they play.

With the advent of "big data" and evolving technology, there are those who believe a computer can provide a more "accurate" opinion of value than appraisers. As these technologies become more refined, it's likely that, in certain cases, that may be true. In areas with extremely homogenous housing and ample sources of market data, a well-written automated valuation model may be a perfectly appropriate way to analyze the collateral on a relatively low-risk loan.

Conversely, there are many markets consisting of properties with varying ages, qualities of construction, condition, levels of renovation, lot sizes, view amenities, etc.—not to mention special financing arrangements or seller concessions. It is in these markets where a professional appraiser is needed to apply the type of *judgment* that a computer cannot replicate. While a computer can do a great job of "crunching" numbers, its output is only as good as its input. If the information required to properly analyze market activity is not entered by a trained professional with a solid understanding of the marketplace, the ensuing results may be suspect.

Having said that, appraisers are poised to be part of the solution; not an obstacle or impediment to sound financial policies. While the type and extent of analyses appraisers will perform is likely to be different than what has been done in the past, seasoned appraisers are some of the best candidates to accurately analyze and interpret market data. While some appraisers fear the emerging technology as a threat to their livelihoods, others embrace it and position themselves to increase their relevancy in the future.

As evidenced by alternative valuation products that have surfaced in today's marketplace, appraisals cannot be "one size fits all." Rather, the extent of analyses and the communication of opinions and conclusions must be flexible. For transactions involving low risk and smaller financial commitments, abbreviated reports that can be performed quickly and at a low cost are needed. Alternatively, lenders considering higher risk investments involving significant capital will continue to rely on more detailed analyses that can be greatly augmented by incorporating new tools and technologies that continue to evolve.

While the marketplace may demand more streamlined products such as Broker Price Opinions, Automated Valuation Models, Desktop Valuations, Comparative Market Analyses, Reconciliation Reviews, etc., who better to perform such transactions than a competent, ethical, valuation professional?

Indeed, financial transactions in the 21st century will be different. And professional appraisers are up to the challenge of meeting the needs of the marketplace.

Conclusion

The Title XI real property appraiser regulatory system, while unique and not without its flaws, has made a positive very real difference over the past quarter century. It is the glue that holds the 55 jurisdictions together and every effort should be made to further refine and improve a system that has demonstrated effectiveness *without the use of appropriated funds.* The Foundation stands ready to assist with this effort in any manner you believe is appropriate.

Appraisers have historically made a significant contribution to the safety and soundness of our financial system and their important role will continue in the future. The catalyst for the creation of the current appraiser regulatory system was to protect the integrity of our deposit insurance system, a need that is as strong today as it ever was.

Again, The Appraisal Foundation appreciates the opportunity to share its perspective with you today and we urge this Subcommittee and all members of Congress to continue to use the Foundation as a fair, impartial and objective resource on valuation-related issues.

COMMON MYTHS ABOUT THE HOME BUYING PROCESS

ATTACHMENT 1

REAL ESTATE BROKERS

MYTH REAL ESTATE BROKERS ARE PROHIBITED FROM COMMUNICATING WITH APPRAISERS.

FACT **Brokers are permitted to communicate with an appraiser and to provide them with additional information as long as the communication is not intended to unduly influence the outcome of the appraisal.** The exchange of relevant information—including terms of the sale, relevant comps, and home improvements—can help an appraiser develop a more credible opinion of value.

MYTH NOTHING CAN BE DONE IF A BROKER HAS CONCERNS OR QUESTIONS REGARDING A COMPLETED APPRAISAL.

FACT **If there are questions or concerns with an appraisal, there are concrete steps brokers can take through the lender,** like submit additional comps for the appraiser to consider, request the appraiser correct errors in the appraisal report, and ask the appraiser to provide further detail to explain his/her conclusion.

MYTH APPRAISERS REQUEST COPIES OF THE PURCHASE AGREEMENT FROM BROKERS SIMPLY SO THEY'LL KNOW HOW MUCH TO APPRAISE THE HOME FOR.

FACT **Appraisers are required to review the purchase agreement (if available during the ordinary course of business) to fully understand the terms of the transaction.** Appraisers don't simply look at a pending sale price and try to "justify" the transaction. They perform research and analyses to provide their own opinion of value.

LENDERS

MYTH A LENDER AND AN APPRAISER CANNOT COMMUNICATE BEFORE, DURING, OR AFTER AN APPRAISAL IS COMPLETE.

FACT **Not only are lenders permitted to talk to appraisers, they must.** Communication is essential for the exchange of appropriate information, including the intended use of the appraisal, the scope of work necessary for credible assignment results, and more.

MYTH NOTHING CAN BE DONE IF A LENDER HAS CONCERNS OR QUESTIONS REGARDING A COMPLETED APPRAISAL.

FACT **If there are questions or concerns with an appraisal, there are concrete steps lenders can take,** like submit additional comps for the appraiser to consider, request the appraiser correct errors in the appraisal report, and ask the appraiser to provide further detail to explain his/her conclusion.

MYTH LENDERS MUST USE AN APPRAISAL MANAGEMENT COMPANY (AMC) TO ORDER AN APPRAISAL.

FACT **Lenders are entitled to engage an appraiser directly.** However, to avoid any potential undue influence on the appraiser, certain safeguards are required (e.g., in most cases the person at the lending institution selecting the appraiser cannot be the same person approving the loan).

MYTH AMCS ARE NECESSARY TO ENSURE THAT APPRAISERS AREN'T INFLUENCED BY LENDERS.

FACT **Regardless of whether an AMC is used, lenders are not permitted to influence the value of a home, and licensed and certified appraisers are required by law to follow strict guidelines** (i.e., the Uniform Standards of Professional Appraisal Practice) that guarantee an unbiased and meaningful analysis of value.

BORROWERS

MYTH AN APPRAISER IS HIRED BY THE BORROWER.

FACT **Even though the borrower may be responsible for the cost of an appraisal, appraisers are hired by lenders.** Appraisers provide an analysis of the collateral, so that lenders understand the value of a property when making the loan decision.

MYTH THE MONEY PUT INTO A HOME TRANSLATES DOLLAR-FOR-DOLLAR INTO A HIGHER APPRAISAL.

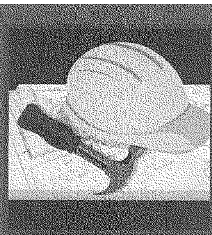
FACT **The cost put into a home improvement project may very well add value to a home; however, the value of any improvements are based on what the market is willing to pay for them, and may not necessarily correlate to the cost.** Not all renovations positively impact property values.

MYTH APPRAISERS SET THE VALUE OF A HOME.

FACT **Appraisers don't set the value of a home, nor do they confirm a home's sale price.** Their role is to produce a credible opinion of value which reflects the current market.

MYTH APPRAISERS AND HOME INSPECTORS PERFORM THE SAME FUNCTION.

FACT **Though both provide crucial information, their roles are very different.** An appraiser provides an objective, unbiased analysis so the lender can better understand the value of a property. An inspector is typically hired by the borrower and performs an objective visual examination of the physical structure and systems of a house to ensure the structural integrity of the property.



HOMEBUILDERS

MYTH HOMEBUILDERS ARE PROHIBITED FROM COMMUNICATING WITH APPRAISERS.

FACT **Builders are permitted to communicate with an appraiser and to provide them with additional information as long as the communication is not intended to unduly influence the outcome of the appraisal.** The exchange of relevant information—including construction features, details, and upgrades, as well as relevant comps—can help an appraiser develop a more credible opinion of value.

MYTH NOTHING CAN BE DONE IF A BUILDER HAS CONCERNS OR QUESTIONS REGARDING A COMPLETED APPRAISAL.

FACT **If there are questions or concerns with an appraisal, there are concrete steps builders can take through the lender,** like submit additional comps for the appraiser to consider, request the appraiser correct errors in the appraisal report, and ask the appraiser to provide further detail to explain his/her conclusion.

MYTH APPRAISERS ONLY RELY ON COMPARABLE SALES AND DO NOT TAKE INTO ACCOUNT THE COST TO BUILD A HOME.

FACT **Appraisers do need to consider the cost to build a home and, at times, must perform a cost approach to deliver a credible appraisal.** However, because cost does not always equal value, appraisers cannot simply look at what it costs to build a home to provide an opinion of value. They must perform research and analyses to determine what the marketplace is willing to pay.

THE APPRAISAL FOUNDATION

Authorized by Congress as the Source of Appraisal Standards and Appraiser Qualifications

www.appraisalfoundation.org

Attachment 2

THE APPRAISAL FOUNDATION

Authorized by Congress as the Source of Appraisal Standards & Appraiser Qualifications

Effective January 2014, rules adopted by the Consumer Financial Protection Bureau (CFPB) allow borrowers to receive copies of all valuation products ordered with their loan (even if the lender did not rely on them) three days prior to closing. Various valuation products (appraisals, AVMs, BPOs) may produce different values and cause confusion for borrowers.

Understanding Valuation Products

A Quick Guide for Borrowers

As a borrower, it is important to understand the differences between the valuation products you may receive before closing on your loan and the relative reliability and applicability of each product. When reviewing valuation products, keep in mind that:

- An **Appraisal** is an opinion of value performed by a professional state-licensed or -certified appraiser. It complies with the *Uniform Standards of Professional Appraisal Practice* (USPAP), which requires appraisers to be independent, objective, and impartial. An appraiser must remain unbiased and produce an opinion of value that is credible, or worthy of belief. An appraisal by a competent professional appraiser is the most reliable of all valuation products.

- An **Automated Valuation Model** (AVM) is a computer-generated estimate of a property's value that a lender might use in some circumstances to assist in evaluating the collateral for a mortgage. The output of an AVM is heavily dependent on the quantity and quality of the data input. With proper use, an AVM can help support the findings of an appraisal, but when used alone its output may not be credible.

- A **Broker Price Opinion** (BPO) is typically prepared by a real estate broker and is another tool a lender might use to evaluate the collateral for a loan. A BPO, as originally intended, does not comply with USPAP, and real estate brokers are not obligated to comply with USPAP and its corresponding appraiser independence requirements. BPOs were designed for brokers to assist home buyers and sellers in arriving at a list or purchase price.

- A **Comparative Market Analysis** (CMA) is similar to a BPO and is commonly prepared by a real estate agent to help decide on an asking or offering price. Like a BPO, a CMA does not comply with USPAP and real estate agents are not required to comply with USPAP.

The Appraisal Foundation, the nation's foremost authority on the valuation profession, has additional resources for consumers. For more information, including A Guide to Understanding a Residential Appraisal, please visit www.appraisalfoundation.org.

1155 15th Street, NW, Suite 1111, Washington, D.C. 20005
Phone: 202-347-7722; FAX: 202-347-7727; Web: www.appraisalfoundation.org

Attachment 3

FEDERALLY RELATED TRANSACTION EXEMPTIONS

§225.63 Appraisals required; transactions requiring a State certified or licensed appraiser.

(a) *Appraisals required.* An appraisal performed by a State certified or licensed appraiser is required for all real estate-related financial transactions except those in which:

(1) The transaction value is $250,000 or less;

(2) A lien on real estate has been taken as collateral in an abundance of caution;

(3) The transaction is not secured by real estate;

(4) A lien on real estate has been taken for purposes other than the real estate's value;

(5) The transaction is a business loan that:

(i) Has a transaction value of $1 million or less; and

(ii) Is not dependent on the sale of, or rental income derived from, real estate as the primary source of repayment;

(6) A lease of real estate is entered into, unless the lease is the economic equivalent of a purchase or sale of the leased real estate;

(7) The transaction involves an existing extension of credit at the lending institution, provided that:

(i) There has been no obvious and material change in market conditions or physical aspects of the property that threatens the adequacy of the institution's real estate collateral protection after the transaction, even with the advancement of new monies; or

(ii) There is no advancement of new monies, other than funds necessary to cover reasonable closing costs;

(8) The transaction involves the purchase, sale, investment in, exchange of, or extension of credit secured by, a loan or interest in a loan, pooled loans, or interests in real property, including mortgaged-backed securities, and each loan or interest in a loan, pooled loan, or real property interest met Board regulatory requirements for appraisals at the time of origination;

(9) The transaction is wholly or partially insured or guaranteed by a United States government agency or United States government sponsored agency;

(10) The transaction either:

(i) Qualifies for sale to a United States government agency or United States government sponsored agency; or

(ii) Involves a residential real estate transaction in which the appraisal conforms to the Federal National Mortgage Association or Federal Home Loan Mortgage Corporation appraisal standards applicable to that category of real estate;

(11) The regulated institution is acting in a fiduciary capacity and is not required to obtain an appraisal under other law;

(12) The transaction involves underwriting or dealing in mortgage-backed securities; or

(13) The Board determines that the services of an appraiser are not necessary in order to protect Federal financial and public policy interests in real estate-related financial transactions or to protect the safety and soundness of the institution.

(b) *Evaluations required.* For a transaction that does not require the services of a State certified or licensed appraiser under paragraph (a)(1), (a)(5) or (a)(7) of this section, the institution shall obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.

(c) *Appraisals to address safety and soundness concerns.* The Board reserves the right to require an appraisal under this subpart whenever the agency believes it is necessary to address safety and soundness concerns.

(d) *Transactions requiring a State certified appraiser*—(1) *All transactions of $1,000,000 or more.* All federally related transactions having a transaction value of $1,000,000 or more shall require an appraisal prepared by a State certified appraiser.

(2) *Nonresidential transactions of $250,000 or more.* All federally related transactions having a transaction value of $250,000 or more, other than those involving appraisals of 1-to-4 family residential properties, shall require an appraisal prepared by a State certified appraiser.

(3) *Complex residential transactions of $250,000 or more.* All complex 1-to-4 family residential property appraisals rendered in connection with federally related transactions shall require a State certified appraiser if the transaction value is $250,000 or more. A regulated institution may presume that appraisals of 1-to-4 family residential properties are not complex, unless the institution has readily available information that a given appraisal will be complex. The regulated institution shall be responsible for making the final determination of whether the appraisal is complex. If during the course of the appraisal a licensed appraiser identifies factors that would result in the property, form of ownership, or market conditions being considered atypical, then either:

(i) The regulated institution may ask the licensed appraiser to complete the appraisal and have a certified appraiser approve and co-sign the appraisal; or

(ii) The institution may engage a certified appraiser to complete the appraisal.

(e) *Transactions requiring either a State certified or licensed appraiser.* All appraisals for federally related transactions not requiring the services of a State certified appraiser shall be prepared by either a State certified appraiser or a State licensed appraiser.

[Reg. Y, 55 FR 27771, July 5, 1990, as amended at 58 FR 15077, Mar. 19, 1993; 59 FR 29500, June 7, 1994; 63 FR 65532, Nov. 27, 1998]

Mortgage Origination Values and Appraiser Credential Trends

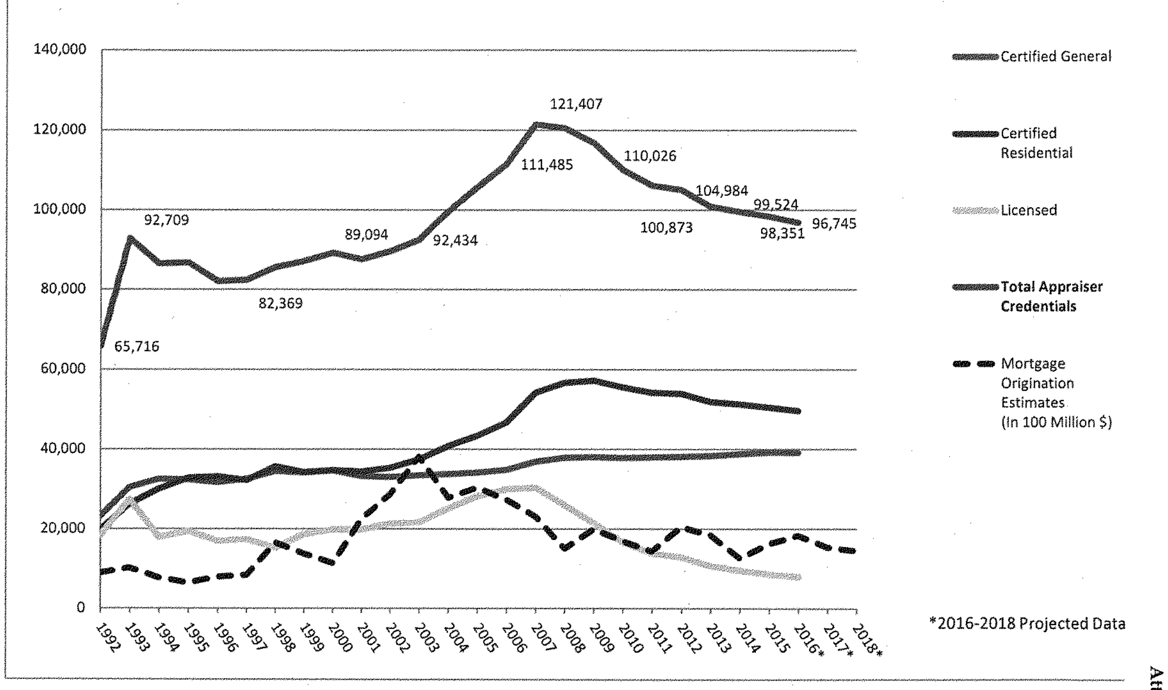


*Chart provided by the Appraisal Subcommittee

Attachment 4

Appraisal Institute®

Professionals Providing Real Estate Solutions

Modernizing Appraisal: A Regulatory Review and the Future of the Industry

Testimony of William E. Garber, Jr.

Director of Government and External Affairs

Appraisal Institute

Before the Subcommittee on Housing and Insurance

House Committee on Financial Services

November 16, 2016

Chairman Luetkemeyer, Ranking Member Cleaver and members of the Subcommittee on Housing and Insurance, thank you for the opportunity to share our concerns and solutions regarding "Modernizing Appraisals: A Regulatory Review and the Future of the Industry" on behalf of the nearly 20,000 members of the Appraisal Institute, the largest professional association of real estate appraisers in the United States.

Real estate appraisal plays a critical role in helping financial institutions conduct risk management and make safe and sound loans. Today, the number of real property appraisers in the United States is in decline, and concerns are being expressed by banks and real estate professionals alike about a potential shortage of appraisers.

What is clear is that all appraisers are being choked by rules and regulations in nearly every facet of their business. From how an appraiser reports an appraisal, to supervising trainees, to uneven licensing requirements, to licensing and registration fees passed down by clients, to mandates from federal agencies – appraisers' professional lives have become extremely complicated, more expensive and less productive due to a dated and archaic regulatory structure. As a result, consumers suffer from increased turnaround time, delays in loans, and potential higher costs.

The Appraisal Institute believes that there is a better, less-complicated approach that would improve appraisal quality, reduce costs, and address fundamental concerns that are driving away today's appraisers from the profession. This model would benefit from the experiences of other industries and precedents established by Congress, resulting in a closer alignment of the appraisal regulatory structure with those found within the real estate and finance industries.

EXECUTIVE SUMMARY

- The federal regulatory structure for real estate appraisal essentially has been untouched since the enactment of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"). Dodd-Frank Act amendments added further complexity to the structure, and the resulting rules are overwhelming practicing appraisers.

- The complicated federal system is proving to be counter-productive for the profession and for users of appraisal services. The Appraisal Subcommittee has veered from its Congressional mandate to audit state appraisal boards for compliance and maintain a National Registry of appraisers in the past to assert authority over the appraisal profession by attempting to add new layers of rules and regulations for appraisers, which ultimately has adversely impacted users of appraisal services, as well.

- Real estate appraisers face a "layering effect" of rules and regulations that create a disincentive for potential entry into the profession, while also diminishing the profession's profitability. This is counterproductive, given that rules continue to grow in number. These include:
  - Background checks with no federal mandate or efficient processing system;
  - Unappealing Supervisory-appraiser and Trainee-appraiser requirements; and
  - Standards that aren't standard at all.

- We suggest Congress modernize the appraisal regulatory structure and realign it with those of other industries in the real estate and mortgage industries, using as a model the National Mortgage Licensing System (NMLS) cooperative among state agencies.

Part 1. The Appraisal Regulatory Structure

Appraiser Population Trends
The Appraisal Institute has analyzed the Appraisal Subcommittee National Registry data since 2006 using consistent methodology.[1] The long-term trend is one of decline in the number of licensed and certified real estate

[1] See U.S. Appraiser Population Estimates, attached.

appraisers in the U.S., with decreases of nearly 3.0 percent annually. (As of June 2016, the total number of active appraisers decreased 22.7 percent compared to the 2007 peak year-end.) A broader analysis, considering these facts and other AI research, suggests the current trend could continue, with the number of appraisers decreasing at a comparable or higher annual rate over the next 5 to 10 years primarily because:

- Age demographics resulting in a high rate of retirements.
- Fewer people entering the real estate valuation profession as evidenced by a dramatic decrease in the number of first-time license and certification test takers.
- Appraisers may leave the profession due to challenging or uncertain business conditions and more government regulation.
- Wider use of alternative valuation technologies may displace some appraisers.
- A potential oversupply of residential appraisers (more than two-thirds of all appraisers focus primarily on the residential sector).

In addition, average fees for residential appraisers have been in decline for many years, while the costs of doing business (I.e., licensing fees, data services, continuing education, reference texts, supplies, vendor fees, etc.) have increased dramatically. When one adds in fee-splitting with appraisal management companies, many residential appraisers actually are making much *less* than they were when FIRREA was enacted. With all of this together, we anticipate a continued decline in the number of practicing appraisers, between 20-25 percent, over the next 5-10 years.

Our data does not indicate a national shortage of appraisers at this time; however, there are indications of shortages in some markets across the country. We anticipate that such shortages would increase should the projected decline fully materialize.

Direct Federal Role

The federal regulatory structure for real estate appraisal essentially has been untouched since enactment of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"). It's safe to say that the marketplace has changed significantly since that time and continues to change rapidly today, which is why the Appraisal Institute applauds Congress for reviewing the current relationship between federal and state responsibilities and how this structure serves consumers, appraisers and other market participants.

Our primary concerns center around the complicated federal system that has proven to be counter-productive for the industry and for users of appraisal services. During prior hearings before this Committee, we have stated our belief that the Appraisal Subcommittee has veered from its original Congressional mandate to audit state appraisal boards for compliance and maintain a National Registry of appraisers to assert authority over the appraisal profession by attempting to add new layers of rules and regulations for appraisers and users of appraisal services[2].

Further, several attempts have been made by The Appraisal Foundation – originally at the direction of the Appraisal Subcommittee – to codify appraisal methodology through a newly-created TAF board, the "Appraisal Practices Board." The Appraisal Foundation attempted to codify methodology through this board in at least three different ways, including a legislative recommendation presented to this Committee during the Dodd-Frank Act deliberations, a proposal to cite works of the Appraisal Practices Board within the Uniform Standards of Professional Appraisal Practice (USPAP[3]) over which it presides, and by allowing state and federal agencies to

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[2] The Appraisal Institute testified in 2011 and 2012 before the House Committee on Financial Services on concerns about the Appraisal Subcommittee's involvement in the creation of the Appraisal Practices Board ("APB"). The APB was created at the direction of the Appraisal Subcommittee – beyond Title XI authorizations. The APB remains a Congressionally-unauthorized board of the Appraisal Foundation, but still has encouraged states to adopt the resulting APB documents for mandatory compliance purposes.

[3] USPAP includes the ethics, development and reporting obligations for appraisers, and it is codified in law in all jurisdictions and referenced in federal bank regulations. Appraisal methodology is found within the body of

adopt the APB's work products in policies and procedures documents. Codification of appraisal methodology threatens practitioners with untold compliance obligations and would stifle innovation within the profession.

Real estate appraisal remains one of the most highly regulated professions in the United States, impacting not only residential real estate appraisers, but also commercial real estate appraisers, and those preparing appraisals in non-mortgage work such as development consulting, litigation support, and tax and financial reporting services, to name a few. Appraisers are regulated by the states, but also are faced with significant federal oversight by the Appraisal Subcommittee. No comparable system of federal regulation or oversight can be found within other real estate or finance industries.

The Appraisal Subcommittee historically has served two primary functions – maintaining a National Registry of real estate appraisers and auditing state appraisal boards for compliance with Title XI requirements. FIRREA puts sovereign state agencies in an awkward position of being audited by a federal agency. Thus, we believe that real estate appraisal is the only industry that contends with such an arrangement or system.

The theory behind a federal agency auditing state appraisal boards has been to ensure that states follow through with development of a certification and licensing system. However, such certification and licensing programs now have been in place for more than 25 years. All states and territories process certifications and licenses and, by the Appraisal Subcommittee's own criteria, no state or territory is at risk of losing status under Title XI requirements.

We have some concerns with the way in which some states conduct enforcement. For example, we find that many disciplinary actions are taken for non-substantive violations, as well as being inconsistently applied from state-to-state. Further, many state agencies lack the financial resources and competency to enforce USPAP for non-federally related transactions. Here, serious consideration should be given at the state level to limiting the scope of state appraisal boards to their original function – mortgage appraisals and federally related transactions. On the plus-side, overall, states' appraiser licensing agencies are performing their base function of processing applications and renewals, and conducting a level of oversight and enforcement – just as other state licensing agencies do in other professional oversight capacities.

However, new rules expected to be issued and finalized next year by the Appraisal Subcommittee quite literally will expand the agency's budget on the backs of appraisers. This new "tax" on appraisers comes in the form of new fees assessed by the Appraisal Subcommittee for inclusion on a registry of appraisal management companies, pursuant to an amendment from the Dodd-Frank Act. In developing the proposed rule, the Appraisal Subcommittee did not consider the impact on small business under the Regulatory Flexibility Act. The likely result will be a pass-through of these registry fees – intended for appraisal management companies – to appraisers. We expect that this will force many small business owners out of the appraisal profession altogether, further exacerbating the shrinking number of residential real estate appraisers.

When Congress passed the Dodd-Frank Act, it clearly intended that this money be used for grants to state appraiser regulatory agencies. However, the Appraisal Subcommittee has made no attempt to establish such a grant system for states. Instead, the Appraisal Subcommittee has utilized The Appraisal Foundation as a conduit for developing state investigator training programs. Thus, according to the proposed rule, the Appraisal Subcommittee intends to utilize this increased revenue to support its underlying Title XI functions – not for a grant program to state agencies.

Lack of Accountability

At a very basic level, the appraiser regulatory structure is overly-complicated and lacks fundamental accountability measures. In its most recent report to Congress, the Government Accountability Office (GAO) identified significant violations of internal control standards by entities that claimed such standards were designed to promote effectiveness and efficiency, and to promote accountability.

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knowledge of real estate appraisal. At its most simplistic level, this includes approaches to valuation, including the sales comparison approach, cost approach, and income capitalization approach and their derivatives.

In January 2012, the GAO released a report citing the need for the Appraisal Subcommittee to establish policies and procedures related to The Appraisal Foundation's funding eligibility. Specifically, the GAO report cited the Appraisal Subcommittee for not having specific policies for determining whether Appraisal Subcommittee grant-funded activities of The Appraisal Foundation are FIRREA-related. The Appraisal Subcommittee's failure to have in place appropriate policies and procedures is inconsistent with federal internal control standards designed to promote effectiveness and efficiency. Further, a lack of such policies and procedures limits the accountability and transparency of the ASC's activities.

The GAO report cites a concern that the Appraisal Institute has shared for many years – that the relationship between the Appraisal Subcommittee and The Appraisal Foundation lacks sufficient accountability measures. Outside of preparing an annual report to Congress, oversight of the ASC and TAF is virtually non-existent. We also note that the Appraisal Subcommittee does not have an inspector general who can conduct independent assessments of either the Appraisal Subcommittee's, or The Appraisal Foundation's, programs and operations.

Background Checks with No Federal Mandate Nor an Efficient Processing System

Appraisers, and those considering entering the profession, must navigate constantly-changing appraisal standards and minimum qualifications. USPAP is modified by the Appraisal Foundation every two years and the *Real Property Appraiser Qualification Criteria* has been under a constant state of change for the last six years. Often the Congressionally-authorized boards of The Appraisal Foundation are indecisive and impose onerous requirements on appraisers only to subsequently modify them or eliminate them entirely, sometimes in the next two-year cycle.

An especially egregious example of this occurred with the addition of the requirement for all new appraisers entering the profession to undergo a fingerprint-based criminal background check. This requirement was imposed by the Appraiser Qualifications Board (AQB) in December 2011 after a series of five Exposure Drafts with an effective date of January 1, 2015.[4] There was no federal mandate for the AQB to take this action.

As a result of this new requirement, and to be sure that they were in full compliance by January 1, 2015, many state appraiser regulatory agencies rushed to their state legislatures to obtain the legal authority necessary to collect fingerprints and conduct the required criminal background checks. Between 2012 and 2014, approximately 36 states enacted new laws and regulations to impose the formal background check requirements on real estate appraisers. Approximately 10 states had existing requirements in place prior to the adoption of the requirement by the AQB in 2011.[5]

In addition to imposing these onerous, new requirements on all new applicants – as was the minimum required by the AQB – many states also imposed similar requirements on existing credentialed real estate appraisers, many of whom had been practicing in good standing without any issues for many years. A few states even went so far as to impose these requirements on appraisers practicing in other states who applied for a license via reciprocity or for a temporary practice permit.

However, by early 2014 the AQB realized that it had erred and that implementation of this new requirement by the states, and acceptance by appraisers, was proving to be more difficult than originally planned. After five additional Exposure Drafts, the AQB finalized significant changes to the background check requirement in March 2015. These changes eliminated the need for appraisers to submit fingerprints and undergo formal background checks. Instead, how a state appraiser regulatory agency determines whether a person applying for an appraiser credential has a background that "would call into question public trust" is rightfully left to the discretion of each state and territory. The mandatory compliance date for state appraiser regulatory agencies also was extended to January 1, 2017.[6]

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[4] "Fifth Exposure Draft of Proposed Revisions to the *Real Property Appraiser Qualification Criteria*" October 27, 2011

[5] http://www.appraisalinstitute.org/ano/ai-report-analyzes-state-rules-on-appraiser-background-checks/

[6] "Fifth Exposure Draft of a Proposed Revision to the 2015 *Real Property Appraiser Qualification Criteria*" January 27, 2015

While the 2015 changes to the background check requirement made by the AQB were favorable, they are not likely to have any effect in reducing regulatory burdens on appraisers and state appraiser regulatory agencies. Approximately 47 states now have requirements in place for formal, fingerprint-based background checks, and it is unlikely that any state will repeal or change its existing requirements. The AQB's indecision between 2011 and 2015 left a system in which appraisers are required to comply with onerous state requirements for fingerprint-based criminal background checks, even though they no longer are required as part of the minimum criteria and were never required as part of any federal law or regulation.

Unappealing Supervisory-appraiser and Trainee-appraiser Requirements

Even the procedures for entering the real estate appraisal profession are driven by complicated rules and mandates. Under the Dodd-Frank Act, The Appraisal Foundation was given purview over supervisory-appraiser minimum qualification requirements. The concern resulting from the financial crisis was of "appraiser mills" where a supervisory-appraiser might have an inordinate number of trainees working underneath him/her and producing appraisals at an unsafe rate. The reaction to this concern was the creation and establishment of more rules for supervisors and trainees – for each to take courses and essentially to lock in the mentor-apprentice relationship that has been found in the appraisal industry for many years.

The benefit of such courses is unclear to us at this point, as the course outline from The Appraisal Foundation is one that essentially is a primer on the appraisal regulatory structure. It has limited practical benefit for either supervisors or trainees, but serves as one additional condition for entering the profession or taking on a new trainee as a supervisor. These processes become even more complicated if an appraiser carries multiple licenses and has trainees in multiple states. While The Appraisal Foundation recently has recognized this as an issue and is attempting to resolve the multi-state supervisor concern, this has discouraged many supervisory-appraisers from taking on new entrants to the profession. It also serves to illustrate how micro-managed appraisal is as a business today.

The Burden of Continuously Changing Standards

Real estate appraisers also face a constantly-changing standards regime that often ties their hands in resolving client needs, while perpetually adding to their regulatory compliance burden. Real estate appraisers must adhere to USPAP when performing federally-related transaction appraisals under FIRREA. Meanwhile, The Appraisal Foundation's Appraiser Qualifications Board mandates that all appraisers take a USPAP course to obtain a certification or license and then complete an "update" course to maintain those certifications and licenses. Further, The Appraisal Foundation requires appraisers to purchase a copy of USPAP ($75) when taking USPAP courses. Thus, not only is USPAP's development funded by a grant from the Appraisal Subcommittee (which, in itself, is funded by fees paid by appraisers – $40 per appraiser to the Appraisal Subcommittee), but The Appraisal Foundation also gets residual revenue from USPAP publication sales compelled by the requirements that TAF alone establishes.

This arrangement is made worse by USPAP's constant maintenance cycles, which ensure a steady "tax" on appraisers, in terms of both publications' sales and mandated courses that must be taken by appraisers to obtain and retain certifications and licenses.

This is in stark contrast with other "standards" processes, which typically update standards only when necessary or under a longer-term perspective. In our view, if standards are well-written, they would not need constant updating, especially on a two-year cycle. Typically, as has been seen in recent years, immediately following the release of a new version of USPAP, proposed changes to the following years' cycle are released for public comment. As it is, The Appraisal Foundation follows a more opportune schedule for updating USPAP, which places a significant compliance obligation – and cost – on appraisers.

In addition, over time USPAP has become "rules-based," versus a document that is principles-focused. This, in part, is in response to state regulatory concerns about attempting to enforce a standard. (The Appraisal Foundation has responded to this by weaving in certain rules for appraisers to follow to assist in enforcement activities). As we discuss below, this inhibits technological development to a degree.

Part 2. Appraisal Independence and Procurement

The Appraisal Institute often hears from real estate agents, home builders and others that real estate appraisals used in conjunction with consumer mortgage financing are "killing deals" and/or holding back the economic recovery of the housing market. These accusations are unfounded and misguided, as appraisers do not "make the market," but rather "analyze and report the market." To this point, real estate appraisals are an important risk management activity to be conducted by banks in making safe and sound lending decisions. Independent appraisals are not meant to simply support purchase contracts – they are obtained to help lenders assess their overall risk.

The Dodd-Frank Act did include an important provision, Section 1472, protecting the independence of real estate appraisers from coercion and intimidation. This should be maintained in any legislative review by Congress.

However, we remain concerned with the overall approach taken by federal regulatory agencies and financial institutions in supporting independent real estate appraisal functions within financial institutions, as well as procedures utilized by lenders, to procure real estate appraisals. Several significant problems are apparent, as follows:

1. The predominant factors in the appraiser selection decision often are the "price" and "turnaround time" of the appraisal, not the quality of service, or geographic or market competency of the appraiser.
2. Federal regulatory agencies remain deeply under-resourced to deal with examination issues involving real estate appraisals. At one point in the 1990s, each federal regulatory agency had competent appraisers on staff helping to support examination teams. Today, there is a grand total of *two* professional designated real estate appraisers supporting examination functions in all three of the major examination agencies. We believe that there is ample room for enhancement, as examiners face a wide variety of collateral valuation challenges today.
3. Federal bank examiners have identified widespread problems with the way in which many banks have handled real estate appraisal administrative duties. A recent review by the Appraisal Institute of Material Loss Reports indicates that 75 percent of now-failed banks previously had been cited for various appraisal violations. These violations included often failing to obtain real estate appraisals where required or having insufficient resources within the bank to manage and oversee the appraisal function.
4. Generally, most banks have opted not to take responsibility or ownership of residential appraisal functions, instead electing to outsource appraisal operations to third parties that offer a perceived layer of insulation from coercive pressure, but apply new business pressures that put constraints on appraisal quality. Many appraisal assignments involving appraisal management companies result in reduced fees to appraisers, as these companies take a portion of the fee for "managing" the process. Further, use of appraisal management companies can add to the time it takes for a bank to finalize appraisal review within a loan application.

Many financial institutions have been under the mistaken impression that federal rules require the use of appraisal management companies to comply with basic appraisal independence requirements. This is not the case, as financial institutions may manage appraisal ordering and review internally. Many financial institutions, upon learning that federal rules allow banks to take back the appraisal function, have reestablished appraisal departments with independent reporting structures as an alternative to utilizing appraisal management companies. Depending on the size of the bank, this may be accomplished with a functioning appraisal department, or hiring an appraiser on staff, or utilizing several available software programs in the market that enable risk management staff to oversee appraisal orders and reviews.

This is not to say that *all* appraisal management companies are performing poorly, because some place the quality of service at the forefront of their business model; it is just that the business model employed by many appraisal management companies has failed significantly. Our biggest concern is the banks' propensity to make appraiser hiring decisions based on speed (or turnaround times) or price, rather than quality or competency (both market and geographic). Here, many institutions appear to ignore federal guidelines that clearly state that price and turnaround time should not be the predominant factors in an appraiser hiring decision. Yet, as cited above, bank regulatory agencies appear understaffed to enforce this provision, helping to enable substandard appraisal procurement by banks.

Technological Advancement in Appraisal

We understand and want to support technological advancement within the appraisal process. Many appraisers are technologically savvy, as data and analysis systems are some of the primary tools used by appraisers. Residential appraisal, in particular, is impacted, perhaps even inhibited, because appraisal report forms and appraisal requirements historically have been confined to the government-sponsored enterprises. Fannie Mae and Freddie Mac maintain and require the use of a suite of appraisal report forms geared to property types, with the *Uniform Residential Appraisal Report (URAR)* being the mostly widely used. These are accompanied by lender and appraiser guidelines found in the Seller/Servicers guidelines that establish parameters around appraisals accepted for loan purchases. The actual appraisal reporting processes – items like quality and condition ratings – for loans sold to the agencies is dictated by the Uniform Appraisal Dataset. Appraisers must follow these rules and now are being evaluated by the GSEs based on how these rules are reported by peers and how they have been previously reported for consistency by appraisers.

The GSE appraisal guidelines and requirements have been and continue to be developed in isolation from the industry. We long have had a level of discomfort with the lack of formal stakeholder input in these processes. Today, the GSE appraisal forms are viewed by many as being out-of-date and in need of a major overhaul or update. The GSE guidelines have had the unexpected effect of actually reducing appraisal quality in some cases, especially for unusual homes or homes in less active markets. Further, the appraisal forms may not be tailored appropriately for the needs of the client community, as the URAR is developed typically with a purchase mortgage transaction in mind. Transactions involving refinance, loan workouts, disposition and portfolio-monitoring likely require a different set of information than what is required by the URAR.

Further, there are changes to appraisal standards that should be explored to allow appraisers to respond to client needs better than they are today. For example, Restricted Appraisal Reports generally are not sufficient for lenders even as "evaluations" because they do not meet the requirements outlined in the Interagency Appraisal and Evaluation Guidelines for either an appraisal or an evaluation. Further, recordkeeping obligations of appraisers actually are greater for Restricted Appraisal Reports. For an Appraisal Report, the supporting data and analysis must be in the report itself, while they must be in the work file with a Restricted Appraisal Report. We believe a more accountable and responsive standards maintenance process would help alleviate some of these problems.

Interim Final Rule & Customary and Reasonable Fees

The Dodd-Frank Act requires creditors and their agents to pay "customary and reasonable" fees to appraisers to reflect what an appraiser typically would earn for a residential appraisal assignment absent the involvement of an appraisal management company. Under the Act, evidence for such fees may be established by objective third-party information, such as government agency fee schedules, academic studies and independent private sector surveys.

In sum, the rules that have been promulgated by the Federal Reserve (Interim Final Rule) and the Consumer Financial Protection Bureau (Final Rule) are not consistent with the plain language and intent of the Dodd-Frank Act. Two presumptions of compliance are provided by the Federal Reserve and accepted by the CFPB that are internally inconsistent. One presumption requires independent studies or fee schedules that align with retail appraisal fees direct from the appraiser, while the other accepts internally generated results that include what amounts to wholesale fees involving third parties.

The CFPB adopted a final rule earlier this year, leaving these presumptions unchanged. We continue to have concerns with the internal inconsistencies found in the two presumptions for compliance, and we urge fresh oversight on this issue and the related issue of consumer disclosure of appraisal and AMC fees, which is outlined below.

Consumer Disclosure

The problem of customary and reasonable fees paid to appraisers is masked by consumer disclosure rules that allow the co-mingling of appraisal and appraisal management company fees on the Appraisal line of the

Consumer Disclosure form issued by the CFPB. This co-mingling confuses consumers into believing that they are paying appraisers more for services today, when, in fact, compensation levels may have significantly declined because appraisal management companies are taking a sizable portion of the total cost paid by the consumer.

The Dodd-Frank Act authorized the CFPB to require the disclosure of AMC fees separate from fees paid to appraisers. In developing the final "TRID" rule, the CFPB conducted consumer testing of sample Closing Disclosure forms. This testing concluded that consumers were indifferent to the disclosure of AMC fees separate from appraisal fees, indicating that consumers were not confused by a disclosed appraisal management company fee. Despite this, the CFPB simply opted to allow disclosure on a voluntary basis, but not mandate it. Today, while some lenders break out the fees paid to AMCs separate from appraisal fees, most do not do so.

Appraisal Threshold Levels

Per the Economic Growth and Regulatory Paperwork Reduction Act, the federal bank regulatory agencies have been reviewing whether to raise appraisal threshold levels, which currently stand at $250,000 for real estate loans and $1 million for business or owner-occupied loans. Testimony on September 28, 2016, by Federal Reserve Chair Janet Yellen to the House Financial Services Committee signaled the agencies' intent to propose a reduction in appraisal requirements, perhaps before the end of 2016. This would reduce fundamental risk management requirements at a time when the housing market only has recently recovered from the largest real estate-related financial crisis in decades, and in the face of numerous alarm bells that have been and still are being sounded by regulators regarding the commercial real estate market.

FIRREA, enacted in 1989 in response to the savings and loan crisis, authorized federal bank regulators to require appraisals for real estate loans made by federally regulated financial institutions. Since that time, the following have occurred:

- In 1994, bank regulators exempted wide swaths of loans from appraisal requirements, including real estate loans below $250,000 and owner-occupied business loans below $1 million. More than 20 years later, a majority of residential real estate loans still do not require an appraisal under the existing exemption.
- The recent financial crisis witnessed widespread problems with bank management of appraisal requirements, including adherence to the 1994 regulations. A vast majority of failed banks from the financial crisis were shown to have been cited by federal bank regulatory agencies for lax appraisal oversight and management.
- In addition to establishing the two appraisal threshold levels in 1994, the agencies exempted loans sold to Fannie Mae and Freddie Mac. This allowance was granted based on a determination by bank regulatory agencies that the government-sponsored entities would maintain equivalent appraisal requirements. In effect, the federal government turned the regulation of residential appraisals over to Fannie Mae and Freddie Mac, who have, in turn, issued guidelines (or rules) with very little input from professional appraisal organizations or stakeholders in general. This has placed a huge responsibility on Fannie Mae and Freddie Mac to "get it right," and they have not in many ways.
- Ultimately, nearly one-third of all loans received an "appraisal waiver." Coupled with poor underwriting and review requirements, the policies of the government-sponsored enterprises drove them into conservatorship by the federal government.
- Since the crisis, the GSEs have required appraisals more often. A 2011 GAO Report found that 85% of mortgages purchased by the GSEs in 2010 were accompanied by appraisals. Today, nearly all first-purchase mortgages require a full interior inspection appraisal completed by a certified appraiser.

Raising the $250,000 threshold level would not affect residential loans as much, as long as Fannie Mae, Freddie Mac and the Federal Housing Administration retain their current appraisal requirements. However, such a move would impact smaller commercial property loans. While each individually might not be that risky, a lender with a concentration of these loans could be faced with considerable risk.

We believe that the appraisal threshold should be maintained at its current level, as a protection against risky real estate lending. This is supported by a survey of our members who work for banks and financial institutions, which resoundingly support maintaining the current threshold levels in support of risk management activities. This survey found:

- A strong majority (76.6 percent) of chief appraisers/appraisal managers strongly or somewhat disagrees with raising the $250,000 threshold level.
- An overwhelming majority (87.5 percent) of chief appraisers/appraisal managers strongly or somewhat disagrees with raising the $1,000,000 owner-occupied commercial real estate threshold level.
- An overwhelming majority (89.1 percent) of chief appraisers/appraisal managers strongly or somewhat agrees that raising threshold levels could increase risk to lenders.
- A strong majority (80.5 percent) of chief appraisers/appraisal managers strongly or somewhat agrees that raising threshold levels could increase risk to borrowers[7].

Part 3. Legislative Reform Options

As Congress reviews appraisal issues, we would like to suggest several reforms to help improve appraiser oversight and enforcement, as well as the overall quality of appraisals.

With regard to the appraisal regulatory structure, we offer the following suggestions:

1. **Realign the appraisal regulatory structure similar to those of other professions in the real estate and mortgage industry. One model that merits consideration is the National Mortgage Licensing System (NMLS), which is a cooperative among state agencies overseen as a last resort by the Consumer Financial Protection Bureau (CFPB).**

2. **Sunset the Appraisal Subcommittee, while maintaining the authorities of state appraisal boards, and align the federal functions with a nationwide portal like the NMLS. This would provide services in one place for appraisal practitioners, appraisers working for financial institutions, and appraisal management companies to apply and renew appraisal licenses and registrations.**

3. **Authorize a federal backstop authority consistent with other regulatory systems authorized by Congress in recent years should states fail to adhere to basic program requirements.**

   Comment: This would simplify the appraisal regulatory structure and make it consistent with others in the real estate and mortgage sectors. Authorizing the appraisal profession to utilize the NMLS for its certification and licensing system would enable state appraiser regulatory agencies to benefit from enhanced communication with other state agencies, including those outside of appraisal, such as state banking regulatory agencies. This enhanced communication among state licensing agencies has been sought for many years by Congress and other observers. Such a system would help state licensing agencies track individuals and firms that may be moving in and out of states after a disciplinary action.

   For example, state appraiser regulatory agencies in Illinois would be alerted immediately if an appraiser was applying for licensure after a disciplinary action was taken in Connecticut. Likewise, state appraiser regulatory agencies would be alerted if a mortgage broker lost his or her license and subsequently was applying for licensure as an appraiser.

   Realigning the appraisal regulatory structure with the NMLS also would provide a common system in which appraisers and appraisal management companies could submit applications for licensure in multiple states. Today, appraisers and AMCs that wish to earn and carry licenses in multiple states must apply in each state separately, significantly adding to administrative requirements and obligations. For instance, appraisers with multiple state licenses must adhere to each state's unique timing requirements and often take the 7-hour USPAP class three or four times a year in order to comply with all the states' requirements. Unlike the appraisal regulatory structure, the NMLS has a common application protocol that is accessed by all of the applicable state licensing authorities.

[7] Available at http://www.appraisalinstitute.org/assets/1/7/Appraisal_Threshold_Levels_Survey.pdf

Interestingly, other industries besides mortgage loan originators are utilizing the NMLS for the very purpose described here. We understand that the NMLS is now accepting other state regulatory agencies into the NMLS. This is because the need for state regulatory information-sharing is not unique to appraisal, but is a widespread issue with many industries. The NMLS has addressed this by offering a solution that may be used by multiple industry regulators.

Should the NMLS fail in its responsibilities to manage appraisal oversight, a specified federal agency (FDIC, FHFA, etc.) should be authorized to step in and administer the appraisal oversight functions, just as it is authorized to do for mortgage loan originators today. This provision established a strong incentive for the NMLS to maintain meaningful programs and operations

.

This is not a proposal to turn the appraisal regulatory structure over to a self-regulatory organization (SRO). SROs typically involve a regulatory system that is administered by *industry*. Here, the NMLS is owned and operated by *regulators*. In addition, the entire NMLS is overseen by a federal agency (the CFPB).

4. **Limit the domain of The Appraisal Foundation to previously-specified areas (standards and qualifications) to ensure that there are no conflicts of interest.**

   Comment: It is common for Congress to establish limitations around the activities of entities recognized in statute. For example, the legislation recognizing the NMLS and the National Association of Registered Agents and Brokers include limitations in the areas of education. These limitations are included to avoid potential conflicts of interest created by the special standing granted in the industry. We believe that similar measures are long overdue relative to The Appraisal Foundation. As an example, The Appraisal Foundation maintains a Course Approval Program that has special standing in the industry that approves appraisal education for its own courses, as well as its competitors.

   Further, we believe that USPAP and the minimum appraiser qualification criteria should be updated on an as-needed basis, not every other year. Practitioners and state enforcement agencies deserve a more stable and consistent standards and qualifications regimen. This would improve enforcement and help improve entry to the profession.

5. **Congress also should prepare for the future of Fannie Mae and Freddie Mac with regard to appraisal policy. Any ongoing federal support or role for either agency, or a future related organization, should maintain consistent appraisal rules like sister agencies such as FHA and VA. Further, we support the establishment of a rulemaking process that would clarify how appraisal services may be used in "subsequent transactions" such as refinancing and loan modifications.**

   Comment: Today, loan servicers often utilize alternative valuation services, such as broker price opinions, out of confusion or a lack of understanding regarding the flexibility of appraisal standards. At the same time, agencies appear unable or unwilling to establish procedures for lenders or loan servicers to engage qualified real estate appraisers to perform more streamlined, or "limited scope" appraisal assignments. Many believe that there is only one type of "appraisal," when, in fact, there are an unlimited number of the types of appraisals, given the ability to tailor the scope of work to a particular client need. If lenders only require a quick update of an original appraisal, appraisers can do this. If obtaining both the market value and the liquidation value of the property would assist with loan review, and determining whether to foreclose or work out the loan, that too could be completed by an appraiser in a cost-effective manner. The agencies should have the ability to establish parameters for obtaining such services from appraisers.

6. **To improve appraisal quality, authorize financial institutions to recognize professional designation programs that exceed minimum licensing requirements.**

   Comment: This would promote professional development within the profession and expose appraisers to advanced education, ethics and enforcement programs.

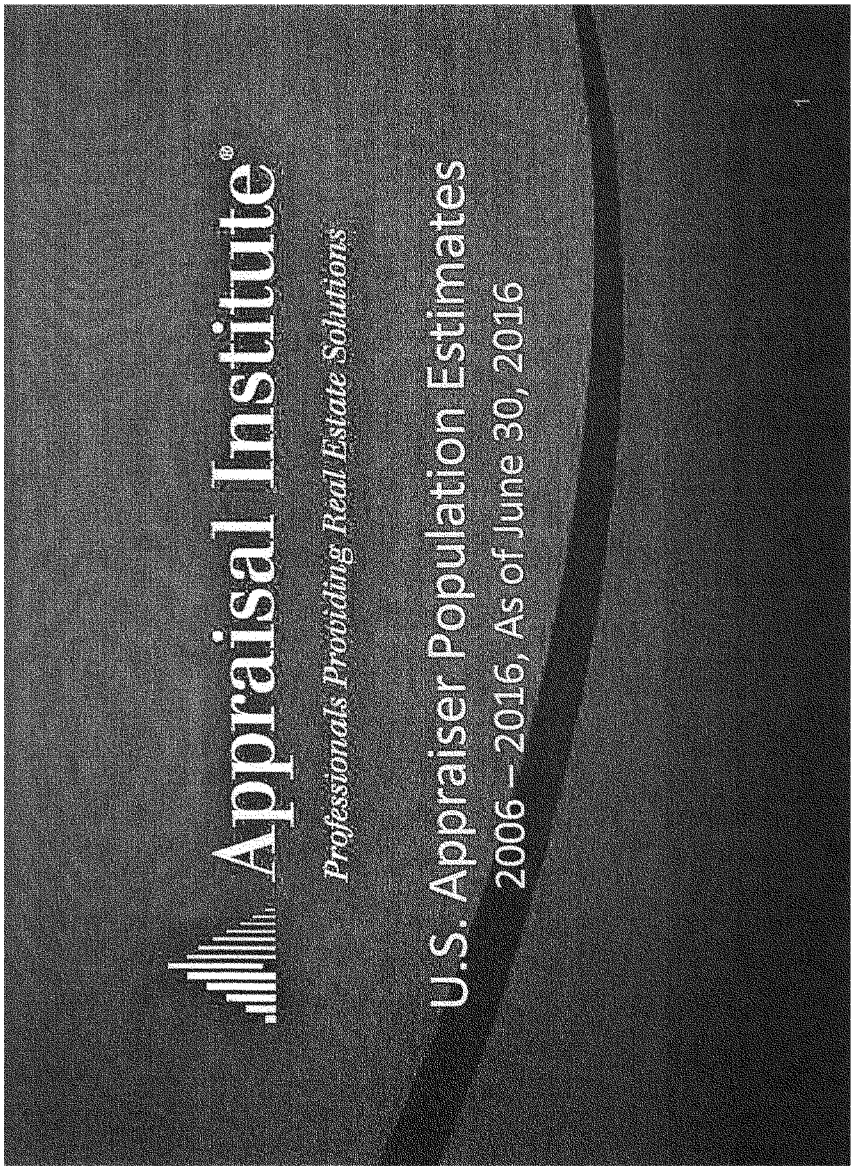
7. **Protect and maintain Dodd-Frank Act, Section 1472, appraisal independence requirements that prohibit coercion and intimidation of appraisers with the full weight of the Truth in Lending Act enforcement provisions.**

8. **Repeal or amend cumbersome sections of the Dodd-Frank Act appraisal amendments.**

   Specifically:
   - The authority for the Appraisal Subcommittee to establish National Registry fees for appraisal management companies. This function would transfer naturally to a NMLS-like system. Such fees should be established at reasonable levels that do not burden small businesses.

   - Mandate separate disclosure of appraisal and appraisal management company fees. Payment of customary and reasonable fees to appraisers for residential appraisal assignments is important to maintaining a system of high quality appraisals. However, the Final Rule's two presumptions of compliance are internally inconsistent. A more straightforward approach would require, and allow, full disclosure of appraisal and appraisal management company fees to consumers.

Thank you for the opportunity to testify on these important matters. I would be happy to answers any questions.


Appraisal Institute®
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U.S. Appraiser Population Estimates
2006 – 2016, As of June 30, 2016
1

U.S. Appraiser Population

As of June 30, 2016

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About the Appraisal Institute

The Appraisal Institute is a global professional association of real estate appraisers, with nearly 20,000 professionals in almost 60 countries throughout the world. Its mission is to advance professionalism and ethics, global standards, methodologies, and practices through the professional development of property economics worldwide. Organized in 1932, the Appraisal Institute advocates equal opportunity and nondiscrimination in the appraisal profession and conducts its activities in accordance with applicable federal, state and local laws. Individuals of the Appraisal Institute benefit from an array of professional education and advocacy programs, and may hold the prestigious MAI, SRPA, SRA, AI-GRS and AI-RRS designations.

U.S. Appraiser Population

As of June 30, 2016

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Methodology

- The source of the data for this report is the Appraisal Subcommittee (ASC) National Registry of Real Estate Appraisers. The data is available for download by the public. Therefore, it is in the public domain and not confidential.
- ASC National Registry archives information on state licensed and certified appraisers; it does not archive unlicensed trainee information. The database contains records of both active and inactive (former) real estate appraisers.
- The Appraisal Institute analyzes the active appraiser portion of the ASC Registry each quarter. The Appraisal Institute uses well-established data mining techniques for removing duplicate or incomplete records on a state-by-state basis. The analysis also identifies appraisers who hold licenses or certifications in multiple states.
- The accuracy of the resulting estimates is 99 percent.

U.S. Appraiser Population

As of June 30, 2016

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Trend

- The Appraisal Institute has analyzed ASC National Registry data since 2006 using consistent methodology. The long-term trend is one of decline in the number of licensed and certified real estate appraisers in the U.S., with decreases of nearly 3.0 percent annually. (As of June 2016, the total number of active appraisers decreased 22.7 percent compared to the 2007 peak year-end.) A broader analysis, considering these facts and other AI research, suggests the current trend could continue, with the number of appraisers decreasing at a comparable or higher annual rate over the next 5 to 10 years primarily because:
  - Age demographics resulting in a high rate of retirements.
  - Fewer people entering the real estate valuation profession as evidenced by a dramatic decrease in the number of first-time license and certification test takers.
  - Appraisers may leave the profession due to challenging or uncertain business conditions and more government regulation.
  - Wider use of alternative valuation technologies may displace some appraisers.
  - A potential oversupply of residential appraisers (more than two-thirds of all appraisers focus primarily on the residential sector).

U.S. Appraiser Population
As of June 30, 2016

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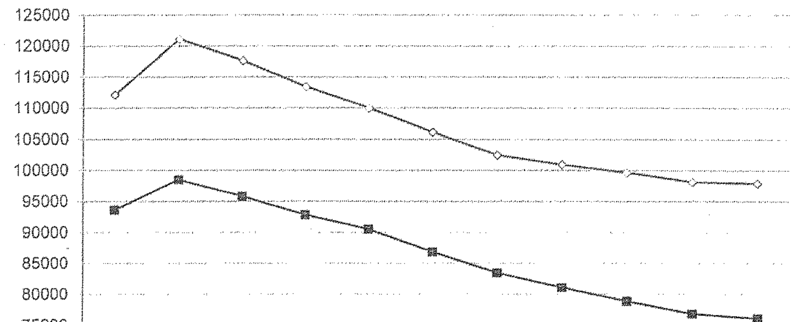
Total Licenses, Certifications, and Number of Appraisers



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Jun-16
Active Licenses/Certifications	112050	121100	117600	113400	109950	106100	102400	100900	99600	98100	97900
Actual Number of Appraisers	93575	98450	95750	92750	90500	86800	83400	81050	78800	76800	76075
Percent Change in Actual Number		5.2%	-2.7%	-3.1%	-2.4%	-4.1%	-3.9%	-2.8%	-2.8%	-2.5%	-0.9%

As of June 30, 2016, the total number of real estate appraiser licenses/certifications decreased by 0.2 percent from year-end 2015. Comparatively, the actual number of active appraisers decreased 0.9 percent for the same period. As of June 30, 2016, the actual number of appraisers decreased 22.7 percent from the peak year-end 2007 level.

U.S. Appraiser Population

As of June 30, 2016

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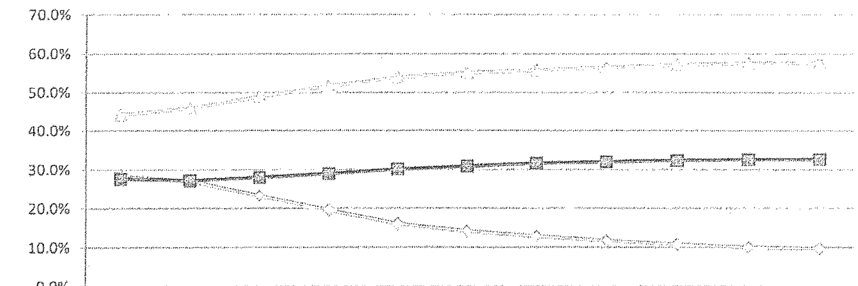
Proportion of U.S. Appraisers Licensed or Certified



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Jun-16
Licensed	28.2%	27.0%	23.2%	19.5%	16.0%	14.1%	12.8%	11.7%	10.7%	10.0%	9.7%
Certified General	27.6%	27.1%	27.9%	28.9%	30.0%	30.8%	31.5%	31.9%	32.3%	32.5%	32.6%
Certified Residential	44.2%	45.8%	48.9%	51.6%	53.9%	55.1%	55.7%	56.4%	57.1%	57.5%	57.7%

As of June 30, 2016, the proportion of Licensed real estate appraisers experienced a minimal decrease while the proportions of Certified Residential and Certified General increased slightly, compared to year-end 2015. The shrinking proportion of Licensed appraisers reflects the overall decrease in the number of trainees and the normal progression from licensed to certified status.

U.S. Appraiser Population
As of June 30, 2016

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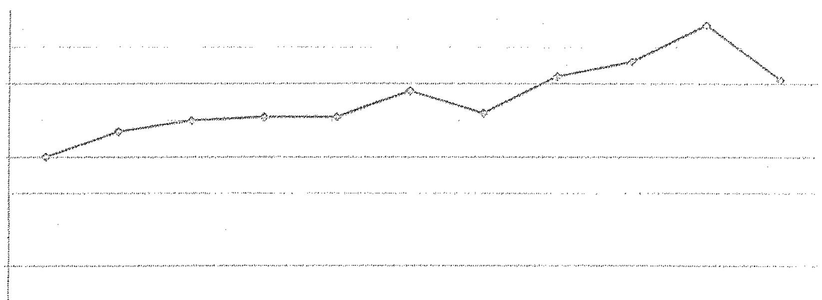
Proportion of U.S. Appraisers Licensed or Certified in Multiple States



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Jun-16
Licensed/Certified in Other States	16.0%	16.7%	17.0%	17.1%	17.1%	17.8%	17.2%	18.2%	18.6%	19.6%	18.1%

As of June 30, 2016, 18.1 percent of real estate appraisers held a license or certification in one or more states/U.S. territories outside their home states/territories.

U.S. Appraiser Population

As of June 30, 2016

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End of Report

Embargoed Until Delivery
10:00 a.m. EDT
November 16, 2016

STATEMENT OF

EXECUTIVE DIRECTOR JAMES R. PARK
APPRAISAL SUBCOMMITTEE
OF THE
FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL

BEFORE THE

UNITED STATES HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES SUBCOMMITTEE ON
HOUSING AND INSURANCE

HEARING ON

MODERNIZING APPRAISALS: A REGULATORY REVIEW AND THE FUTURE OF THE INDUSTRY

NOVEMBER 16, 2016

I. Introduction

As Executive Director of the Appraisal Subcommittee (ASC), I appreciate the opportunity to address the Subcommittee on the Federal appraisal regulatory structure and respond to the specific discussion topics as requested. This statement will first provide history of the appraisal regulatory structure and the creation of the ASC in response to the savings-and-loan crisis of the 1980s. Next, the statement will describe the ASC's core functions and operations pursuant to Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (Title XI). The statement will then discuss the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) on the appraisal regulatory system. The Dodd-Frank Act amendments to Title XI authored by former Members of Congress Judy Biggert and Paul Kanjorski changed numerous provisions related to the ASC's operations, role and responsibilities. Finally, the statement will respond to the specific discussion topics as requested.

II. History of the Appraisal Regulatory Structure

Title XI created the ASC as an entity within the Federal Financial Institutions Examination Council (FFIEC), although the ASC for the most part operates independently of the FFIEC. In general, the ASC oversees the real estate appraisal regulatory framework as it relates to federally related transactions. The Federal and State appraisal regulatory framework governing federally related transactions includes any real estate-related financial transaction that a Federal financial institutions regulatory agency[1] or an institution regulated by such an agency engages in or contracts for, and requires the services of an appraiser.[2]

Following the savings-and-loan crisis of the 1980s, Congress passed Title XI to address identified weaknesses in the appraisal profession and the credibility of real property appraisals

[1] The Federal financial institutions regulatory agencies consist of the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency.
[2] Title XI § 1121 (4), 12 U.S.C. 3350, as amended.

supporting the lending activity of federally regulated institutions. Title XI recognized the need for uniform appraisal standards and minimum qualification criteria for appraisers. Prior to Title XI, appraisers were, for the most part, unregulated at either the Federal or State level. There was no generally accepted set of uniform appraisal standards. Congress found that the appraisal profession was fragmented with only one third of appraisers having a membership with a professional appraiser organization. Congress also found that those professional appraiser organizations disciplined their members on an infrequent basis.[3] Today, still only roughly one third of appraisers are members of professional appraiser organizations. The federal financial institutions regulatory agencies had broad safety and soundness guidelines requiring regulated financial institutions to consider the nature and value of a loan's collateral. Title XI sought to address this situation with an emphasis on the importance of appraisals to support safe and sound real estate lending activity of federally regulated institutions and to protect Federal financial and public policy interests in real estate transactions.

Title XI created a unique regulatory framework for real estate appraisals and appraisers that involves Federal, State and private entities:

- At the Federal level, the ASC provides Federal monitoring, support and oversight to both the private and State entities, while the Federal financial institutions regulatory agencies are responsible for prescribing appropriate standards for the performance and use of real estate appraisals in connection with federally related transactions under their jurisdiction.
- At the State level, State regulatory agencies are responsible for the certification, licensing and supervision of appraisers.
- On the private side, the Appraisal Foundation (Foundation), a private non-profit corporation, is responsible for promulgating uniform appraisal standards and minimum

[3] Title XI 48th Congressional Report by the Committee on Government Operations (Sept 25, 1986).

real property appraiser qualification criteria. The Foundation serves as the parent organization for two boards established to accomplish this mission: the Appraisal Standards Board (ASB) and the Appraiser Qualifications Board (AQB). These boards respectively promulgate and maintain the Uniform Standards of Professional Appraisal Practice (USPAP) and the Real Property Appraiser Qualification Criteria (AQB Criteria).[4] In turn, the ASC is authorized to provide grant funding to defray costs associated with these two boards.

III. ASC Core Functions and Operations

Pursuant to Title XI as amended, the ASC monitors the requirements established by States for the certification and licensing of appraisers qualified to perform appraisals in connection with federally related transactions. Specifically, States must adopt and/or implement all relevant AQB Criteria for the certification and licensing of appraisers.

Title XI requires the ASC to monitor both the requirements established by the Federal financial institutions regulatory agencies (agencies) with respect to appraisal standards for federally related transactions under their jurisdiction, and the agencies' determinations as to which federally related transactions under their jurisdiction require the services of a State certified or licensed appraiser. Pursuant to ASC policy, ASC staff meets annually with member agency representatives for a briefing on the public actions taken by the agency. The results of those briefings are reported in the ASC's annual report to Congress.

The ASC is further required to monitor and review the practices, procedures, activities and organizational structure of the Foundation. In monitoring the Foundation, ASC staff attends all public and private meetings of the Foundation boards, including their Board of Trustees. ASC

[4] The AQB Criteria establish the minimum requirements for credentialing of appraisers qualified to perform appraisals for federally related transactions, including education (for initial qualification and continuing), experience and examination.

staff also reviews and comments on proposed and final published documents regarding the AQB Criteria and USPAP when appropriate. ASC staff also attends meetings of the Appraisal Practices Board (APB) as part of the responsibility to monitor activities of the Foundation. No grant funds are awarded to the APB as Title XI only authorizes grants to the Foundation for the work of the ASB and AQB.

The ASC is required to maintain a National Registry (Registry) of State certified and licensed appraisers who are eligible to perform appraisals for federally related transactions. Through the Registry, State and Federal regulators, lenders and consumers can determine whether an appraiser holds an active credential in good standing with the State, the type of credential and the State disciplinary history for that appraiser. The Registry became operational in 1992 and is available on the ASC website (www.asc.gov). Over the years, system enhancements have been made to the Registry to improve public access. The Registry allows authorized and properly trained personnel from each State to update, in real time, a State's Registry submission and disciplinary actions taken against its licensed or certified appraisers. The Registry contains approximately 96,500 appraiser credentials which represent approximately 79,000 individual appraisers. The ASC is in the process of developing a unique identification number for each appraiser on the Registry. Once fully implemented in all 55 States (*i.e.*, 50 States, District of Columbia and four Territories), the identification number will link appraiser credentials on the Registry so that an appraiser's credential in one State will be linked with that same appraiser's credential in any other State. It will also allow the ASC to discontinue use of personally identifiable information and improve the consistency and reliability of the Registry.

The ASC is solely funded by the Registry fees. In order to be on the Registry, appraisers pay an annual $40 Registry fee. That fee is paid to the State and passed through to the ASC.

Pursuant to Title XI, amounts appropriated for or collected by the ASC shall be used, among other things, "to make grants in such amounts as it deems appropriate to the Foundation, to help defray those costs of the Foundation relating to the activities of the Appraisal Standards and Appraiser Qualifications Boards."[5] Since making its first grant in 1992, the ASC has made over $20 million in grant funds available to the Foundation. The grant defrays the expenses of grant-eligible activities such as the development and maintenance of USPAP, the AQB Criteria and the National Uniform Licensing and Certification Examinations. The Foundation submits an annual grant request to the ASC for grant-eligible activities of the ASB and AQB and is reimbursed for grant-eligible activities on a monthly basis. Further, the ASC engages an independent public accounting firm to review the Foundation's grant-eligible activities and the monthly reimbursement requests.

The ASC also provides grants to the States as required by the Dodd-Frank Act. At this time, the State grant is for the development, presentation and hosting of State Investigator Training Courses. The courses, which are developed jointly by the Foundation, the States, and the ASC staff and administered by the Foundation, provide training to assist States in investigating complaints against appraisers. The courses cover topics such as USPAP and proper investigative techniques, include three course levels, and provide resources to aid the States in their processing of complaints against appraisers. Since the introduction of the courses in 2009, they have been well attended and highly rated by the students. They appear to have a positive impact on the States' compliance with Title XI, particularly in improving the timely resolution of complaints. Investigator training is an excellent example of the successful partnership that has developed and strengthened over the past 25 years between the States, the private sector and the ASC.

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[5] Title XI § 1109 (b) (4), 12 U.S.C. 3338, as amended.

A key responsibility of the ASC is to monitor and assess State appraiser regulatory programs for compliance with Title XI. State appraiser regulatory programs are reviewed every two years, at a minimum, through an on-site Compliance Review process. Compliance Reviews are scheduled to coincide with a meeting of a State appraiser regulatory program's decision-making body whenever possible, and are conducted over a two- to four-day period. ASC staff assesses the State appraiser regulatory programs for compliance with Title XI, ASC Policy Statements[6] and AQB Criteria. The ASC's Compliance Review of the State appraiser regulatory programs focuses on three key components of Title XI: (1) implementation and enforcement of USPAP and the AQB Criteria; (2) adequacy of the State's statutory or regulatory authority, funding and staffing to successfully carry out Title XI-related functions; and (3) consistency with Title XI in the decisions of the State appraiser regulatory programs.

The ASC issues a final Compliance Review Report and letter to the State with a determination regarding the State's compliance with Title XI. In 2013, the ASC changed the rating system for assessing State compliance with Title XI from a somewhat ambiguous rating system whereby State appraiser regulatory programs were found to be either: (1) in substantial compliance; (2) not in substantial compliance; or (3) not in compliance[7] to a clearer rating scale of: Excellent, Good, Needs Improvement, Not Satisfactory or Poor. Based on the most recent Compliance Review results, States are currently rated as follows: 18 Excellent, 24 Good, 13 Needs Improvement, and no States are rated Not Satisfactory or Poor. The improved rating system has resulted in States being encouraged to be diligent in their efforts to comply with Title XI and rewards them when they are successful.

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[6] The ASC periodically issues Policy Statements to assist the States in understanding the ASC's expectations for State appraiser regulatory programs. The Policy Statements reflect the general framework that the ASC uses in the Compliance Review process.

[7] In Substantial Compliance – Applies when no issues of non-compliance or violations of Title XI, ASC Policy Statements or AQB Criteria are identified. Not in Substantial Compliance – Applies when there are one or more issues of non-compliance or violations of Title XI, ASC Policy Statements and/or AQB Criteria but the concerns do not rise to the level of "not in compliance." Not in Compliance – Applies when the number, seriousness or repetitiveness of the Title XI, ASC Policy Statements and/or AQB Criteria violation warrant this finding.

The general areas of non-compliance with Title XI and the number of States experiencing those problems are presented in the 2015 Annual Report available on the ASC website (www.asc.gov). A summary of those findings over the past two years is also included in Appendix B of the 2015 Annual Report.

Title XI authorizes the ASC to take action against a State in the case of non-compliance with an order of non-recognition. Such an order would effectively mean that federally regulated financial institutions would be unable to conduct real estate lending in a non-compliant State as institutions would be unable to employ the State's licensed or certified appraisers. Not only would federally related transactions be impacted, but the secondary mortgage market, which generally requires the services of a State licensed or certified appraiser for transactions they purchase and securitize, would also be severely and negatively impacted. For those reasons, States have had a significant incentive to comply with Title XI.

The ASC is made up of seven members as designated by the heads of the Federal financial institutions regulatory agencies, the Department of Housing and Urban Development, the Federal Housing Finance Agency and the Consumer Financial Protection Bureau. These are, for the most part, the largest and most influential federal regulators that impact mortgage and commercial real estate lending. The ASC is headquartered in Washington, DC and currently employs a staff of 12. For the 2017 fiscal year, the ASC recently approved a budget of $3.9 million which includes $659,000 in grants to the States and Foundation.

IV. Dodd-Frank Act Impact on the Appraisal Regulatory System

The Dodd-Frank Act included an emphasis on consumer and residential mortgage lending, recognizing that appraisals provide important information on a property, including its market value, that assists consumers in making informed borrowing decisions, as well as providing important information for the lender to understand the risk in a real estate loan. A credible appraisal performed by an independent appraiser provides consumers with an additional safeguard against predatory lending.

With the enactment of the Dodd-Frank Act, the amendments to Title XI expanded the ASC's authority and provided additional tools for the ASC in carrying out its responsibilities.[8] Significant changes include:

- The requirement to transmit an annual report to Congress not later than June 15 of each year that describes its activities during the preceding year. The 2015 Annual Report has been submitted to Congress and is available on the ASC website (www.asc.gov).
- Added ASC authority to take interim action against a State in the case of non-compliance with Title XI (as an alternative to, or in advance of non-recognition).
- The Dodd-Frank Act directed the ASC to establish an advisory committee of industry participants, including appraisers, lenders, consumer advocates, real estate agents, and government agencies, and hold meetings as necessary to support the development of such regulations. In February 2014, the ASC constituted such an Advisory Committee. The Advisory Committee met four times over the next year and delivered their recommendations to the ASC in May 2015. The ASC is considering the Advisory Committee's recommendations for future rulemaking.
- The Dodd-Frank Act required the ASC to oversee State registration and supervision of Appraisal Management Companies (AMCs) and develop and maintain a National Registry of AMCs. On June 9, 2015, the Federal Reserve Board, Comptroller of the Currency, Federal Deposit Insurance Corporation, National Credit Union Administration

[8] Title XI § 1103.

and Federal Housing Finance Agency (the Agencies) issued the final rule, Minimum Requirements for Appraisal Management Companies, to be applied by States that voluntarily elect to register and supervise AMCs. On May 20, 2016 the ASC issued a proposed Rule to implement collection and transmission of annual AMC registry fees. The comment period was 60 days and we received 103 comments. The ASC is now working on the Final Rule. After the AMC registry fee is established, the ASC will launch the National Registry of AMCs.

- The Dodd Frank Act required the ASC to establish a Hotline to refer complainants to appropriate State and/or Federal agencies that handle alleged violations of the Uniform Standards of Professional Appraisal Practice (USPAP) and/or appraisal independence requirements. The Hotline was established in March 2013. Since then, the Hotline has been used well over 18,000 times and produced over 600 referrals to Federal agencies and over 2,000 referrals to State agencies. Prior to the launch of the Hotline, consumer and other stakeholders had little way of knowing where to find the right agency or agencies to assist them with an appraisal-related complaint.
- The ASC was required to hold ASC meetings in open session after notice in the Federal Register. The ASC now holds open meetings which are frequently attended by industry observers.
- The CFPB and FHFA were added to the ASC. Given the importance of these agencies to the mortgage lending industry, adding them to the ASC has given the ASC a more well-rounded perspective on the particular appraisal issues facing consumers and mortgage lenders.

Regarding the future of appraisal oversight, it is critical that the partnership between the States, private sector and ASC remains intact. Although the system has been in place for 25 years, it is still a relatively new and unique regulatory structure. In fact, it is a structure that should be viewed as model for other occupations. In the initial period following the enactment of Title XI, there was significant disagreement, and to some degree, dissension among the States, Foundation and ASC. Since that time, a great deal of effort has been made to strengthen these relationships and it has been effective. Today, all three stakeholders meet regularly and work together on various projects and issues. Examples include collaboration between the States, the Foundation and the ASC on State investigator training as discussed above, and in 2013, the collaboration to develop a "Voluntary Disciplinary Action Matrix" in an effort to promote more consistent disciplinary guidance for appraiser regulatory programs. It was very well received by the States, and although not required, it is frequently used by States as a gauge to determine if their discipline is similar to other States.

V. Discussion Topics

- Explore alternative home valuation methods that could simplify the home buying process:
  - Alternative valuation methods have been used in mortgage lending for many years. For example, for select transactions, the GSEs use alternative valuation products (e.g. proprietary automated valuation models) and have used these products for close to 20 years. The use of differing appraisal/valuation products

in the mortgage lending process should be tied to the risk characteristics of a loan. As more and more appraisal/property data is collected and becomes available to appraisers and others, opportunities for new and improved streamlined valuation products are likely to be developed. Nonetheless any statistical model will, lack expert judgement, and by the nature of modeling itself, be incorrect a certain percentage of the time. When statistical models are applied to a population of loans the errors of over- or under- valuation will offset one another. Any error, of course, will not be offset if applied to a single transaction.

  - Care should be taken not to over emphasize the simplicity of the home buying process. A home is the largest purchase in many consumers' lifetime and many consumers rely on industry professionals for assistance. Virtually all of these professionals profit from the transaction based solely on its outcome. The appraiser, on the other hand, is the only independent professional in the transaction who is not compensated based on the value or the outcome of the transaction. Adequate protection of the consumer and the safety and soundness of the U.S. financial system should be the primary concern.

- Address the appraiser shortage and the impact of licensed versus certified appraiser requirements:

  - I am not aware of any definitive studies or data that indicate there is a systemic shortage of appraisers on a national basis. Certain parts of the country (e.g. Oregon, Washington, and Colorado) and some rural markets have reported a significant surge in demand due to local economic factors. However, there has yet to be a study completed that reveals the reasons for these localized supply and demand issues. ASC staff has continually worked closely with all the States over the past 25 years. During that time span, ASC staff has become aware of localized appraiser supply and demand issues in various parts of the country at different times. For example, significant decreases in interest rates frequently lead to surges in demand and extended appraisal completion times. Those problems have been largely temporary, and once the market cools, supply and demand returns to normal. In fact, nationally, an oversupply of appraisers has been a more common complaint than a shortage. Even today, there may be an oversupply of appraisers in certain areas. During the Compliance Review process, States for the most part have indicated they believe any current shortages of appraisers is temporary and due to historically low interest rates or other local economic factors.

- I am, however, concerned about the lack of entrants into the appraisal profession versus the numbers of appraisers retiring or leaving the profession for other reasons. This has been a trend for several years now and could lead to shortages in the future. Trainee appraisers are required to find mentors with whom they must apprentice and experienced appraisers may be reluctant to train new appraisers. The AQB is currently proposing various approaches to ease the minimum qualification criteria required to obtain a license or certification.
- Many appraisers often refuse mortgage lending assignments due to what they feel is inadequate compensation and other work related conditions or issues.
- In 2008, Congress passed the Housing and Economic Recovery Act (HERA). This Act barred FHA from accepting appraisals performed by licensed appraisers.

It is not uncommon for licensed appraisers to be located in and perform rural appraisal assignments. Those appraisers may also engage in other professional activities, such as real estate sales, due to the lower number of transactions in those markets as compared to suburban and urban markets. Since appraisal is not their primary or only source of income, many of these licensed appraisers never saw the need to move up to become a certified appraiser. Since HERA, many lenders have followed suit and will not allow licensed appraisers (or trainee appraisers) to perform appraisals for their institutions. As a result, approximately 8% of the appraiser population has effectively been eliminated from the mortgage lending process.

- Apply and set the de minimis value threshold required for Federally Related Transactions:
    - The Federal financial institutions regulatory agencies set the de minimis threshold with CFPB concurrence based on statutory authority. Questions regarding the de minimis threshold should be directed to those agencies.
- Streamline the current federal regulatory regime
    - The current structure for appraisal regulation has become more streamlined and effective. Over the past 25 years, the partnership between the Foundation, States and ASC has grown and developed into an excellent example of how the private sector, States and federal government can work together toward a common goal. In the case of appraisal regulation, that goal as stated in Title XI, is to protect public policy interests in federally related transactions. The ASC recognizes the

importance of a streamlined regulatory regime. To that end, over the past several years the ASC has:

- Revised and issued new Policy Statements providing clear and concise guidance to State appraiser regulatory programs for compliance with Title XI.
- Implemented a new and improved rating system with clearer metrics that provides an incentive for States to improve their programs and strive for excellence.
- Implemented a revised Compliance Review Report format with clear and direct feedback to State regulators.
- Reduced Compliance Review turnaround times from over 200 days on average to less than 60 while maintaining a quality process.
- Improved the functionality of the National Registry of Appraisers. The National Registry was upgraded several years ago to allow users of appraisal services to download the Registry data electronically. This has significantly improved the usefulness of the Registry and the speed of downloading data into user's own applications. Since the upgrade, hits on the Registry have increased over 100% to roughly 1.2 million hits per month.

Related areas that could be streamlined or improved:

- Standardize the varying requirements placed on appraisers by the GSEs, FHA, VA, and the Federal financial institutions regulatory agencies. New appraisal report forms should be developed that only require the appraiser to provide relevant and less superfluous information. New report forms could be developed that would provide more meaningful data analysis for lenders and the secondary market.

- Stabilize appraisal standards and the minimum qualification criteria for credentialing of appraisers with less frequent change. Regulators (State and Federal), lenders and appraisers should partner to develop new appraisal/valuation products that utilize the data that is now being collected by the GSEs and others. Currently that data is largely used as a tool for quality control of appraisals.

- Lenders and regulators should reconsider how appraisals are used in the 21st century mortgage lending market place. Requiring an appraisal to provide one specific value creates a barrier to lending that need not exist. Appraisers should be able to provide a reasonable range of value that would allow the lender to appropriately assess risk. Currently, the value in the appraisal may be slightly less than the value needed to "make the deal work." This may result in a low risk transaction being denied, or the borrower may have to put more money down, or in the case of a purchase transaction, the seller could be asked to reduce the negotiated contract price.

- Finally, please discuss whether the current federal regulatory system – including the Appraisal Subcommittee – should be replaced with a State-based regulatory structure and what impact such a change would have on consumers and the mortgage finance system.
    - Over the past 25 years, the current appraisal regulatory structure has developed into a cohesive system that draws on the strengths of the States, private sector and Federal government. The system also relies on appraisers to regulate other appraisers. For example:
        - Most States have appraisers on their Board and/or their staff.
        - The Foundation relies on appraisers to populate their Boards.
        - The ASC, as a result of the Dodd-Frank Act, is now required to have at least one appraiser on its Board.
        - The ASC, is fully funded by appraiser paid National Registry fees to support the work of the ASC, as well as providing the resources for significant grants to the States and Foundation.
    - Removing the Federal regulatory structure and replacing it with a State-based regulatory system would greatly complicate, not streamline the system. It would likely increase costs to consumers and lenders and unnecessarily burden the mortgage finance system for the following reasons:
        - The current structure includes uniform standards and minimum qualification criteria established by the ASB and AQB respectively, and enforced by the ASC. States must implement or adopt these uniform

standards and minimum qualification criteria. As a result, States share a common baseline and are, in large part, prevented from establishing greatly varied statutes and regulations that apply to appraisers, and by extension, to mortgage lenders.

- Without the federal underpinning, over time, States would likely implement significantly dissimilar approaches to appraisal regulation which could increase regulatory burden and costs on companies involved in mortgage lending on a multi-State basis. This could also lead to increased safety and soundness concerns for financial institutions as they would be forced to manage inconsistent and varied appraisal-related statutes and regulations across the country. This might unravel the long-held objective of making mortgage loans fungible in order to be able to sell loans to investors, which in turn, provides a stream of needed funding for new loans across the U.S.

- A State based regime may complicate the GSE and securitization market, which favor standardization. As a result, investors may perceive more risk which could negatively impact the pricing of securities.

- Efforts of organizations such as the Mortgage Industry Standards Maintenance Organization (MISMO) to standardize the data elements used in residential and commercial property transactions could be significantly set back.

- There are numerous examples of States creating differing statutes and regulations in areas outside of Title XI. For example, lenders and AMCs frequently complain that appraisal reviews are not covered by Federal law and the States regulate appraisal reviews in various ways. Some States require that an appraisal review be performed by someone credentialed in the State where the subject property is located. Other States only require a credential when the appraisal review includes an opinion of value (an appraisal). And, some States have no statutes or rules regarding appraisal reviews. Another example is evaluations. Although allowed by the Federal banking agencies in certain cases, evaluations are not covered by Federal law. Therefore, States have varying requirements for evaluations, including barring their use or essentially requiring that an evaluation be performed as an appraisal by an appraiser. The varying laws and regulations by States add to the level of confusion. Confusion creates uncertainty which leads to added regulatory burden and expense.

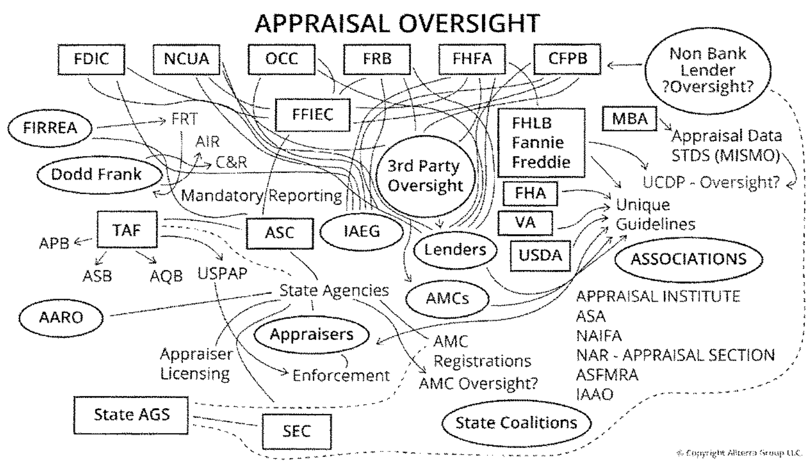
- Another good example is in the area of licensed appraisers. Prior to the Dodd-Frank Act, States did not have to comply with minimum requirements established by the AQB. This led to inconsistent requirements in the States for licensed appraisers and confusion among the stakeholders. Licensed appraisers were perceived to be less competent and more likely to be involved in fraud or misrepresentation. Ultimately several States removed the licensed category and Congress, in 2008, barred FHA from accepting appraisals from licensed appraisers. This is a perfect example of the chaos that could ensue without a Federal baseline.

VI. Conclusion

Without the uniform standards and minimum qualification criteria promulgated by the Foundation and enforced by the ASC, States would very likely institute significantly disparate requirements leading to an increase in regulatory burden, expense and uncertainty for lenders, appraisers and others that have a multi-State business model. While I fully appreciate and support States' rights to govern themselves and regulate occupations that practice within their States, I also recognize the importance of having a national minimum baseline for appraisal standards and appraiser qualifications to facilitate commerce. Dismantling the system could lead to unintended consequences such as increased mortgage lending costs for lenders and consumers as well as an increased potential for added risk and fraud in real estate lending transactions. In conclusion, the appraisal regulatory system envisioned by Congress in 1989 and implemented in 1991 has developed into an excellent example of cooperation between the States, private sector and Federal government all working toward a common goal; broadly speaking, public trust in the appraisal profession.

Modernizing Appraisals: A Regulatory Review and the Future of the Industry
Testimony of Joan N. Trice, SRA
Before the Subcommittee on Housing and Insurance
November 16, 2016

Chairman Luetkemeyer, ranking member Capuano and members of the Subcommittee on Housing and Insurance, thank you for the opportunity to share my thoughts regarding "Modernizing Appraisals: A Regulatory Review and the Future of the Industry".



Today, all stakeholders suffer from an appraisal regulatory regime that is outmoded. The housing finance crisis shed a bright light on the systemic failures of the appraisal process. The structural flaws of the regulatory schema reveal a system whereby no one was held accountable. This illustration of the current regulatory structure says it all.

It should be no surprise that given the above diagram, that the appraisal industry is being highly scrutinized. It is entirely dysfunctional. It is time for a "big and bold" plan to overhaul the system.

The appraisal profession needs a single authority to take ownership of the policy, process, practice, and procedures and the people. National licensing is needed with oversight at the state level. States must adopt a standardized process for investigation and adjudication of any disciplinary actions. Peer review and rehabilitation of the appraiser should occur at the state level.

This new entity should not carry forward any of the legacy agencies that exist today. The times calls for a fresh, holistic solution to replace the disjointed, ineffective structure that currently exists. Repeal FIRREA and replace it with this new independent agency.

Independence is the cornerstone of the appraisal process. HVCC and subsequently the AIR (appraisal independence requirements) components of Dodd Frank left an indelible mark on the appraisal profession. For the past 9 years practically every stakeholder has done their best to avoid compliance with AIR.

Appraisal is truly the weak link and our current policies and systems continue to diminish the important role that appraisers play in the housing finance ecosystem. Discussions of shortages, poor quality, cost, delayed delivery of appraisals, and the de minimus threshold are all code for efforts to further diminish the role of the appraisal process.

The events of the presidential election offer a cautionary tale. Big data failed. Models failed. Bias and lack of independence by the analysts failed. Fannie Mae and Freddie Mac would have you believe they hold all of the marbles. Once again they are competing with each other by reducing appraisal requirements. This is a race to the bottom. We've seen this movie before and we know how it ends. Do not think for a minute that you can replace appraisers with push button technology. Appraising is part art and part science. Create a system, whereby well trained, ethical appraisers have access to reliable data and afford them the independence to play their important role.

If Congress is truly serious about the safety and soundness of the housing finance system, then there is only one clear path for the appraisal process to thrive—establish a single authority over real estate appraisal.

The white paper entitled "Reengineering the Appraisal Process, Revisited" explores in greater detail solutions to bolster the appraisal profession. Thank you for the opportunity to share with you my thoughts on this important topic.

Reengineering the Appraisal Process

July 4, 2016

Joan N. Trice

Introduction

One of the leading causes of the largest housing finance crisis in history was the failure of the appraisal process to produce credible appraisal reports and to identify risks. We are fast approaching the ninth year anniversary of Fannie Mae and Freddie Mac being placed into conservatorship. The Government Sponsored Enterprises (GSEs), for the most part, were the custodians of the appraisal process.

An indelible moment in the history of the appraisal profession was the imposition of the Home Valuation Code of Conduct (HVCC) upon the Government Sponsored Enterprises (GSEs) and their then regulator, Office of Federal Housing Oversight (OFHEO) by the New York Attorney General's (NYAG) office.

The signing of this agreement in 2008 was essentially an admission that appraisal independence had been violated. The GSEs reliance upon "reps and warrants" for appraisals from their servicer sellers was revealed to be a major vulnerability. There was "trust" without the all-important second phase of "verify".

It was generally not known that Fannie Mae and Freddie Mac did not receive appraisal files with the loan origination files. The GSEs securitized trillions of dollars of loans, collateralized loans based upon, in part the valuation, without any verification of a single data point from the appraisal. This is how Uniform Collateral Data Portal (UCDP) was borne. The NYAG and Fannie Mae and Freddie Mac's regulator agreed to launch an appraisal repository to begin the process of monitoring appraisal quality to satisfy the demands for adherence to appraisal independence.

Appraisals are an integral part of the housing finance system. Some of the challenges in the appraisal process have been improved with components of Dodd Frank and new guidance from the Federal Financial Institutions Examination Council (FFIEC) agencies. The regulatory schema is complicated and the oversight is lacking or uneven at best. Order out of chaos could be established with the transition to a single valuation regulator with a clear set of rules and standards.

The appraisal process needs to be structurally reorganized within a single authority. This new regulator, The Collateral Risk Foundation would establish a Collateral Valuation Advisory Committee comprised of multiple housing stakeholders and a Valuation Board comprised of regional chief appraisers to better serve dynamic markets.

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Failures of the Appraisal Process

The problems that plague the appraisal profession are many and complex. It is time to modernize and rethink the practices, policies and procedures for appraisals. Many of the failures of the current the system emanate from a regulatory schema that is complicated and ineffective. Data and technology infrastructure is woefully lacking. We also failed to provide oversight of the people-part of the process to remove bad actors from the system.

Date & Technology

Given that residential real estate is the largest asset class in the world, it is astounding that so little information is available on the very "sticks and bricks" that are the underlying collateral for a mortgage loan. There is no inventory of U.S. real estate; no national database. And because of that lack of aggregated data and transparency there remains little confidence demonstrated by private secondary market participants to invest in mortgage backed securities.

Even today, loan applications collect loads of information on the borrower but nothing beyond a postal address on the property. Appraisers are sent appraisal requests for a single family loan that may, for example, be multiple homes on a single deeded 10 acre lot, one well and septic with a commercial auto body garage. No one on the front end qualified the property. This makes TILA- RESPA Integrated Disclosure (TRID) difficult to comply with and places blame on the appraiser for delays and/or for the delivery of a report that will never be pristine. It is the property, not the appraiser, at fault in this scenario.

In Spain for example, the borrower submits physical characteristics including square footage, any recent additions, permits, improvements and receipts of the property and recent photographs. The information is transmitted to several appraisers who bid on the property. The client weighs the experience, fee and delivery and places the order. It is worthy to note that in Spain the educational requirement for appraisers is that of an engineer, a six year degree. And they are compensated at an equivalent of approximately $800 per assignment.

Structural Defects

The Appraisal Subcommittee (ASC) was established according to Financial Institutions Reform and Recovery Act (FIRREA) Title XI in 1989. The ASC provides for the federal oversight of state appraisal agencies. These state agencies are responsible for licensing of appraisers and oversight. On July 21, 2010, the President signed into law the Dodd-Frank Wall Street Reform and

Consumer Protection Act of 2010 (Dodd-Frank Act) that includes amendments to Title XI. Dodd Frank added new responsibilities to state agencies that included the registration and oversight of Appraisal Management Companies (AMCs).

Appraisal Management Companies (AMCs) proliferated post HVCC when it was assumed that the use of an AMC created a firewall between loan production and the appraiser. Unfortunately it would appear that some banks as well as non-bank lenders established their own AMCs to control the appraisal process and thwart appraisal independence. The oversight of AMCs is now a responsibility of the state appraisal agencies that are ill equipped to handle such a tremendous responsibility. We have merely offloaded the risk now to third party entities under the watch of agencies who have little funding or skills to do so. The numbers of illegitimate businesses that have been established to pervert the system is an unquantifiable risk event in the making. Appraisal independence problems have not been eliminated, they have just been redirected.

From the vendor side of the equation legitimate AMCs are systematically punished by a system where they will be required to register in each state through a different system and process, each with a new set of fees, renewal dates and unique state laws. This is an untenable system where the bad actors can flourish and honest, competent private enterprises get punished. The unintended consequences of this system have yet to be fully played out. As of this date 38 states have AMC registrations in place.

The Appraisal Subcommittee (ASC) is an independent agency that is a subcommittee of the Federal Financial Institutions Examination Council (FFIEC). This has created an inverted pyramid. The ASC reports to the FFIEC whereas ideally an appraisal agency should be independent of the bank regulators and should be promulgating a set of standards and rules by which banks and non-bank lenders should comply.

Modern housing finance is a national activity, not a local one, yet we have a regulatory schema that appears to be neither effective nor scalable. Licenses should be issued at a national level, with local oversight. This oversight needs to be evenly applied. Many lessons can be learned by a review of other systems that do work. In Germany, for example, what is equivalent to state boards monitor the work product of each licensee and offer guidance and mentorship programs to elevate the quality of appraisals. If a licensee fails to improve through these mentorship programs and education they are removed from the system.

Fannie Mae and, to a lesser degree, Freddie Mac bear some responsibility for the breakdown of the appraisal process. The appraisal process is essentially owned by the GSEs. In a void with no central authority Fannie Mae became the de facto standard bearer for the valuation profession. Regardless of the ultimate future of the GSEs, the appraisal process should be established in an independent entity.

Process, Practice, Policy

There are two fundamental reasons for the breakdown in the appraisal process. First, the definition of "market value" is highly flawed. A lot of blame has been placed upon appraisers for failing to report credible values during the crisis. Appraisers have simply been asked to produce an estimate of "market value" as currently defined. The second issue is the reporting format itself. The current residential appraisal report forms, dictated by Fannie Mae and Freddie Mac, are archaic in every sense of the word.

Definition of Market Value

The debate over the challenges created by the definition of market value has been increasing but only in the subtext. This definition was promulgated in 1989 in FIRREA. The definition prior to the Savings & Loan Crisis included language that used "highest probable price" rather than " most probable".

Market value is the most probable price that a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

- *buyer and seller are typically motivated;*
- *both parties are well informed or well advised, and each acting in what he or she considers his/her own best interest;*
- *a reasonable time is allowed for exposure in the open market;*
- *payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto; and*
- *the price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.*

Other countries have successfully implemented the concept of a sustainable lending value as opposed to market value. Values can be subject to wild fluctuations creating havoc in the mortgage lending environment as we have just experienced. The precept of a "mortgage lending value" decreases the impact on short-term volatility by focusing on sustainable values for the life of the mortgage loan.

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The use of the term "price" within the definition "value" is an underlying problem. These two terms are not interchangeable. Mortgage lending should be based on value, not price. The perfect example is during the years preceding the mortgage meltdown, house prices in Las Vegas were inflating at a rapid rate. The role of the appraiser was to report three recent sales on a grid. That was easy. No fraud was involved for an appraiser to include three recent settled sales. Nowhere within the reporting format controlled by the GSEs, was the appraiser asked to identify any risks associated with such outrageous trends. It was fairly obvious that these trends were not sustainable.

Had a definition of a "mortgage lending value" been the promulgated definition, perhaps the bubble would have at least been moderated. Another safeguard would have been the application of the three approaches to value. Fannie Mae dropped the requirement for the appraiser to develop the cost approach in 2005. A redesign of the reporting format to include access to and analysis of broader market metrics would be a first step towards a more credible appraisal report.

Solutions

There is not a singular challenge nor is there a monolithic solution to a reengineering of the appraisal process. The modern appraisal theory and practice was born out of the 1930s. Major catastrophic events seem to be the only influencer to the appraisal system. It has taken decades to grow and emerge as a fundamental and necessary component of the housing finance system yet it has taken less than a decade for Fannie Mae and Freddie Mac to systematically diminish and unravel the fundamentals of the appraisal process.

The current regulatory structure is complicated, and unresponsive. If the role of the appraisal community is to act as the "brakemen" to an overheated market the multiple regulatory entities today have not and cannot function in this manner.

The Collateral Risk Foundation's primary activities would be to:

1) create appraisal reporting formats
2) institute policy around the appraisal process
3) establish a data repository to warehouse all valuation reports
4) explore the science of collateral risk

Structure

The Collateral Risk Foundation would establish a Board of Directors, from the various stakeholder groups, to govern the operations of the entity and provide oversight and control. The Collateral Risk Foundation could be an arm of a cabinet level agency of Real Estate Department (RED). RED could be the agency that establishes the data standards and protocols for a national registry of all real estate with a unique geocoded identifier. This would establish the foundation for the "real estate super highway" that must be built.

The Collateral Risk Foundation could emulate the Federal Reserve with a board of regional chief appraisers, the Valuation Board. This would accommodate reporting at a regional and local level for real estate market risk indicators. Having measurable information in real time would allow lenders to offer products and services to consumers that are risk based.

The Collateral Risk Foundation could also support a Collateral Valuation Advisory Board comprised of the many stakeholders within housing finance to include the National Association of Home Builders, National Association of Realtors, Mortgage Bankers Association, American Bankers Association, the Appraisal Institute, US Mortgage Insurers, and capital markets participants and so on.

Repository

The mission of creating a database of all appraisals would be to monitor risk and contribute to a broader housing finance ecosystem that ensures safety and soundness. By establishing data standards, improving the data collection and reporting by appraisers, and making available transactional level information, all stakeholders, including consumers, would benefit.

In addition to creating a repository for all appraisals, a credentials registry of appraisers should also be included. All actors in the transaction should be registered to monitor behaviors between appraisers, lenders, AMCs and so on. Access to these patterns of behavior helps to identify fraud and vulnerabilities to appraisal independence. Implicit in this credentials registry would be integration of an AMC Registry. All credentials would be validated at time of registry of a transaction. Such a system does exist at Clearbox. Clearbox is a credentials database of all licensed appraisers and all known AMCs. Each has been assigned a unique identifier.

A chain of title for all appraisals would be logged. If a loan is sold, access would be granted based upon permissions established by the seller. Much of the fraud and misadventures committed in the past had been based upon lack of transparency. Appraisal independence was grossly abused whereby lenders would order multiple appraisals until they could obtain one at a high enough number to satisfy the loan requirements. Mortgage Backed Securities (MBS) were essentially dark pools. Millions of dollars of loans within a portfolio were sold with little access to any data from the appraisal. This still transpires today including securities sold by the GSEs.

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The Repository would prevent these unsafe lending practices in the future. All stakeholders would have access to better information on the front end of a transaction. They would also be able to monitor markets in real time. The Repository would help restore confidence in the underlying valuations on loan portfolios and individual loans, and in the process help restore the public confidence in the financial services marketplace.

An examination of the European system reveals some interesting facts. Germany has experienced the lowest default rate of any country. In Europe there are a number of triggers for a new appraisal. While the Europeans have very different real estate markets, there are lessons to be learned. Any event triggers a new valuation. An event is considered:

- A non-performing loan
- Establishment of a REIT
- Purchase
- Refinance
- Portfolio transactions
- Syndications
- Taxation
- Securitization

New Appraisal Forms

In order to have access to better data to be able to make better collateral risk decisions it would be necessary to deconstruct and rebuild the appraisal forms currently owned and controlled by Fannie Mae and Freddie Mac. The VA and FHA also adhere to the use of the GSE standard forms with a few addendums of their own.

The current forms do not address many of the data elements necessary for lenders, investors, insurers and rating agencies to perform adequate analysis of the underlying valuation and risk. There are also superfluous data points that need to be jettisoned. For example, it is doubtful that the identification of window type, such as double hung, is a meaningful data element for anyone. There are property characteristics however that are not collected that impact property risk. For example, the age of the roof, the age of the furnace, replacement windows, and other energy efficient items are not adequately addressed. In today's lending environment we place the highest risk borrowers in the highest risk properties. If we addressed this systemic problem we can create meaningful solutions. One might be to calculate a "reserves for replacement" adjustment to offset a potentially catastrophic repair.

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A lot of the problems with the appraisal process begin with the form. It is the form that drives the process. One of the goals of the Collateral Risk Foundation would be to establish the business requirements of the new reporting format. The technical solutions would be developed by independent software companies to design field data collection applications, a smart form, regression tools, risk tools and modular reporting formats.

Science of Collateral Risk

Collateral Risk is a term hardly mentioned in a post mortem analysis of the demise of the housing finance system. That could possibly be explained away by a lack of understanding and access to data. After all, we rely heavily on credit scores on the credit risk side of the equation.

Once the Repository of appraisals is established the possibilities for research and the development for collateral risk tools are endless. There would be the opportunities to harvest new construction costs, land costs, rental information, inventories, property characteristics and so on. From this information would come the ability to analyze trends and develop leading indicators, risk flags and collateral risk scores.

Rational policies and practices could be established based upon what is gleaned from big data. If it can be proven from the data that certain property types yield lower risk of default, new products could be developed and policy written to better assist the underserved markets.

The burgeoning science of Behavioral Economics tells us that consumers don't always behave rationally. We want to build a system that results in regulators writing rational policy and lenders making rational loan decisions. If a homeowner wants to pay a price for a home, regardless of the value, that should be their prerogative. But we should not allow a system to promote the inflation of appraised values at the expense of the health of the overall economy. Inflating values while simultaneously increasing Loan-to-Value ratios is a recipe for disaster. It produces a negative compounding effect of misaligned incentives.

Conclusion

If the housing finance system is to move forward progressively and safely, solutions to the valuation component need to be put forth. In fact, while Congress prolongs the debate on the future of the GSEs it becomes increasingly apparent that a single regulator and authority over all things valuation is essential.

History is certain to repeat itself if we fail to recognize mistakes committed during the largest financial collapse ever. The failure of global economies was a fire

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sparked by the housing market meltdown. The housing crisis was caused, in part but certainly not wholly, by a collateral valuation process that was corrupted by:

- a lack of transparency
- lack of independence
- the systematic marginalization and dismantling of the appraisal process
- and weak oversight

In conclusion the Collateral Risk Foundation should be established to be that entity to be the independent, custodian of the appraisal process. A holistic solution serving all stakeholders would set us on the right path for returning confidence in the markets for consumers as well as investors.

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Testimony before the United States House of Representatives

Committee on Financial Services

Housing and Insurance Subcommittee

Hearing on
"Modernizing Appraisals: A Regulatory Review and the Future of the Industry"

November 16, 2016

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Also on behalf of:
National Consumer Law Center (on behalf of its low-income clients)
National Association of Consumer Advocates

Chairman and Members of the Committee, on behalf of Mountain State Justice, the National Consumer Law Center, and the National Association of Consumer Advocates, thank you for inviting me to testify today regarding the appraisal industry, the Dodd-Frank Act's impact regarding appraisals, and the future of appraisals.[1] I am the Managing Attorney of Mountain State Justice, a non-profit legal services provider in West Virginia that exclusively represents low-income people at no cost to them. Since the early 2000s, we have served thousands of homeowners in danger of losing their homes as the direct result of appraisal fraud and other predatory lending practices.

I am here today to thank Congress for imposing stricter standards for appraisals under the Dodd Frank Act. As I will explain, these new standards have dramatically reduced fraudulent appraisals, in turn saving tens of thousands of homeowners from foreclosure.

It is common knowledge that lax regulation of the mortgage and appraisal market led directly to the financial collapse of 2008.[2] Prior to that collapse, unscrupulous mortgage brokers and lenders joined forces with a handful of appraisers to fraudulently inflate home values to enable property flipping schemes and other home-secured lending of increasingly large amounts. Many of these loans contained adjustable rate or interest only features that would cause payments to skyrocket after a teaser period. Even before the market collapse in 2008, consumers and their advocates began to see this house of cards topple, as homeowners trapped in these underwater loans were unable to refinance when their adjustable rates spiked.[3] Thousands—and soon millions—of homeowners faced foreclosure.[4]

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[1] More information about **Mountain State Justice** can be found at www.mountainstatejustice.org.

The **National Consumer Law Center** is a nonprofit organization specializing in consumer issues on behalf of low-income people. Since 1969, the nonprofit National Consumer Law Center® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness.

The **National Association of Consumer Advocates** is a non-profit organization whose members are private and public sector attorneys, legal services attorneys, law professors, and law students whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers by maintaining a forum for information sharing among consumer advocates across the country and serving as a voice for its members as well as consumers in the ongoing effort to curb unfair and abusive business practices.

[2] *See, e.g.*, The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States, available at https://www.gpo.gov/fdsys/pkg/GPO-FCIC/content-detail.html.

[3] Mountain State Justice's Executive Director testified before this Subcommittee in 2005 about these very practices. *See* Daniel F. Hedges, *Testimony before the Subcommittee on Housing and Community Development*, Committee on Financial Services, U.S. House of Representatives (Sept. 29, 2005), available at http://archives.financialservices.house.gov/media/pdf/092905dh.pdf.

[4] The Financial Crisis Inquiry Report: *Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States 402*, available at https://www.gpo.gov/fdsys/pkg/GPO-FCIC/content-detail.html.

This bubble in housing prices was not just created by a spike in consumer demand. Rather, in many cases throughout country, it was created as the direct result of intentional fraud and lack of oversight. West Virginia—which saw little increased demand—is a prime example of this. At my organization alone, every week we saw dozens of homeowners facing foreclosure resulting in large part from these fraudulent appraisals.

The Dodd-Frank Act required essential increased regulation of appraisals, building on necessary safety and soundness requirements passed after the savings and loan crisis. These recent changes have been instrumental in ending the practice of fraudulent appraisals, primarily by requiring appraisal independence. Appraisal independence ensures that lenders and brokers cannot intentionally choose appraisers who will deliver implicitly (and sometimes explicitly) requested inflated appraisals. Reforms requiring true, in-person appraisals by qualified appraisers similarly have ensured not only a healthy appraisal industry, but also that lenders and investors can be certain that they have sufficient collateral to protect their risk. These reforms have been an unqualified success. They have worked.

Because the reforms did exactly what they were intended—they stopped appraisal fraud—we urge you to leave these requirements in place. Appraisal oversight does not just help consumers, it also supports honest appraisers and lending institutions, and protects investors and the economy as a whole.

Background

Home appraisals are required to safeguard homeowners, home mortgage investors, and government insurance programs alike. Appraisals protect homeowners who are making the largest investment—and taking on the largest debt—of their lives, by enabling them to make wise and well-informed financial decisions. Appraisals are necessary to ensure that loans do not exceed the values of homes that serve as their collateral. This collateral protects investors and insurers, such as the Federal Housing Authority, against the risk of long-term home lending. Provision of sufficient collateral thus enables and supports lending, which in turn creates a healthy housing market.

Home appraisals are supposed to be conducted by highly trained and skilled professionals with knowledge of the local area. Appraisals, under current standards, require the appraiser to personally view both the interior and exterior of the home, the surrounding area, and comparable homes that have recently sold on the open market, in order to ensure an accurate opinion of value. Appraisers are educated in a classroom and serve as an apprentice under the supervision of an experienced appraiser before they obtain their final certification. All of these requirements ensure that appraisers are qualified and competent to complete their essential work.

Widespread Appraisal Fraud[5]

Without independent and qualified appraisals, home secured lending poses significant risks to consumers, investors, as well as the entire economy. Two main types of appraisal fraud in particular led to the market collapse in the 2000s: property flipping scams and refinance fraud.

Property Flipping

Property flipping scams involve speculators who buy dilapidated residential properties or develop shoddy new construction at low prices and resell them to unsophisticated first time home buyers at huge markups.[6] Homeowners end up saddled debt load that exceeds the market value of the property. These homeowners are unable to resell the home in an arms-length transaction because the mortgage indebtedness exceeds the fair market value of the property. Ultimately, the homeowners may lose their homes due to foreclosure sales[7] because the home's condition is much worse than represented, promised repairs are not performed, and the consumer's mortgage payments may be higher than the consumer can afford.[8] Then the scams can begin again against different homeowners if the wrongdoers or their confederates purchase the homes at the foreclosure sales.

An inflated appraisal, which is necessary to both reassure the homeowner and to secure an inflated loan, is the linchpin of these transactions.[9] While many property flipping schemes rely on steering borrowers to high-cost lenders,[10] other schemes depend on the availability of government insurance.[11] Because Federal Housing Administration (FHA) insurance, unlike regular mortgage insurance, covers 100% of lender's losses, lenders quickly profit from inflated loans they know will foreclose.[12] The loan officer gets a commission; the Department of Housing and Urban

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[5]Significant portions of the following text, especially background on appraisal fraud, the mortgage market, and regulatory overviews are drawn from the National Consumer Law Center's book on mortgage lending, National Consumer Law Center, *Mortgage Lending* (2d ed. 2014).

[6] *See, e.g.*, Synovus Bank v. Karp, 887 F. Supp. 2d 677 (W.D.N.C. 2012); Kaing v. Pulte Homes, Inc., 2010 WL 625365 (N.D. Cal. Feb. 18, 2010), *aff'd*, 464 Fed. Appx. 630 (9th Cir. 2011). *See also* Upton Sinclair, The Jungle 77–78 (1920) (describing a scheme in which a developer repeatedly sold poorly constructed homes, foreclosed on them, and then resold them as "new").

[7] *See, e.g.*, United States v. Geig, 176 Fed. Appx. 638, 639 (6th Cir. 2006) (upholding restitution award and prison term for participant in property flipping scheme that "left buyers with overvalued properties with a high risk of foreclosure"); David Cho, Housing Boom Tied to Sham Mortgages, Lax Lending Aided Real Estate Fraud, Wash. Post., Apr. 10, 2007, at A1 (more than 300 homes go into disrepair and foreclosure in wake of property flipping scheme, surrounding homeowners lose as much as half of the value of their homes).

[8] *See* Edmonds v. Hough, 344 S.W.3d 219 (Mo. Ct. App. 2011).

[9] *See* United States v. Owens, 301 F.3d 521 (6th Cir. 2002) (describing appraiser's key role in a property flipping scheme); Vaughn v. Consumer Home Mortg. Inc., 2003 WL 21241669 (E.D.N.Y. Mar. 23, 2003).

[10] *See, e.g.*, United States v. Sheneman, 2012 WL 1831660 (N.D. Ind. May 18, 2012); Edmonds v. Hough, 344 S.W.3d 219 (Mo. Ct. App. 2011).

[11] *See, e.g.*, Vaughn v. Consumer Home Mortg., Inc., 293 F. Supp. 2d 206 (E.D.N.Y. 2003); Consumer Prot. Div. v. Morgan, 874 A.2d 919 (Md. 2005).

[12] *See* M & T Mortg. Corp. v. White, 2006 WL 47467 (E.D.N.Y. Jan. 9, 2006) (finding predatory lending scheme was caused in part by HUD's issuance of insurance without due diligence); Vaughn v. Consumer Home Mortg., Inc., 293 F. Supp. 2d 206 (E.D.N.Y. 2003) (denying HUD's motion to dismiss declaratory judgment that FHA insurance was issued without due diligence). *See also* LaBoy v. Better Homes Depot, Inc., 2004 WL 6393656, at *8 (E.D.N.Y. July 14, 2004) (recognizing role of FHA insurance in property flipping scheme involving inflated appraisals).

Development (HUD) is left with the costs associated with the bad loan.[13] Some of these scams landed their perpetrators in prison after the market collapse. Others just led to disastrous consequences for homeowners.

Many of Mountain State Justice's clients suffered from these dynamics. For example, the S family is extremely low-income and had never before owned a home, but were desperate to find a safe place for themselves and their five children. In 2007, Mr. and Mrs. S family visited a loan officer at a national lender that had a storefront office in their community, and were preapproved for a loan. Mr. S then located a home and contacted the lender. The loan officer promptly contacted an appraiser from a different region of the state who reliably inflated appraisals, and provided her with the requested target figure. The S family purchased the home for $35,000, based on the resulting appraisal. Little did they know that the home had evident defects that any appraiser should have recognized, including exposed wiring, significant leaks, termites, mold, dryrot, and sewage leaking in the basement. I met the S family when they faced foreclosure because they could not afford to keep up with the loan payments—which had an interest rate over 9% and exceeded their prior rental payment—or make necessary repairs on the home to keep their family safe. They also could not sell the home because the loan far exceeded its value. They never would have purchased the home or entered the loan if the appraisal had noted these facially evident safety hazards.

Bogus Refinances

In addition to being the linchpins of property flipping schemes,[14] inflated appraisals are also the key to predatory mortgage refinances that directly led to the 2008 market collapse.[15] For instance, loan churning, which involves repeated refinancing with additional fees and costs rolled into the new principal balance, often depends on inflated appraisals to justify higher loan amounts.[16] Without the inflated appraisal, these loans would be denied for insufficient equity.[17]

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[13] *E.g.,* Saucier v. Countrywide Home Loans, 64 A.3d 428 (D.C. 2013); Hoffman v. Stamper, 867 A.2d 276 (Md. 2005).

[14] *See* United States v. Curtis, 635 F.3d 704, 709 (5th Cir. Mar. 11, 2011) ("Obtaining inflated appraisal reports was a critical leg of the conspiracy."); United States v. Owens, 301 F.3d 521, 528 (6th Cir. 2002) (describing appraiser's key role in a property flipping scheme); Vaughn v. Consumer Home Mortg., Inc., 2003 WL 21241669 (E.D.N.Y. Mar. 23, 2003).

[15] *Cf.* Wallace v. Midwest Fin. & Mortg. Services, Inc., 714 F.3d 414, 422 (6th Cir. 2013) (reversing summary judgment for broker and lender on civil racketeering claims based on an inflated appraisal of borrower's home; noting, "Though the decision to obtain a mortgage is no doubt complicated, the appraisal of the home used to secure it is a fundamental part of the calculus.").

[16] *See, e.g.,* Hill v. Meritech Mortg. Services, Inc. (In re Hill), 2002 WL 34560882 (Bankr. E.D. Pa. Sept. 27, 2002).

[17] *See, e.g.,* Wallace v. Midwest Fin. & Mortg. Services, Inc., 714 F.3d 414, 417 (6th Cir. 2013) (inflated appraisal "factored significantly into" the underwriting of the loan; discussing importance of inflated appraisal to conspiracy to sell borrower a high-interest rate loan with high fees); United States v. Rivera, 2004 WL 3153171 (D. Conn. Aug. 5, 2004); Chavarria v. Fleetwood Retail Corp. of N.M., 115 P.3d 799 (N.M. Ct. App. 2005) (affirming judgment against manufactured home seller based on fraudulent conduct of two employees in inflating trade-in value of borrower's previous manufactured home and including fictitious home improvements in the loan amount; reducing duplicative damages and reversing award of punitive damages), aff'd in part, rev'd in part, 143 P.3d 717 (N.M. 2006) (affirming judgment against seller but reversing compensatory and punitive damages award); Office of the New York State Att'y Gen., Press Release, N.Y. Attorney General Sues First American and Its Subsidiary for Conspiring with Washington Mutual to Inflate Real Estate Appraisals (Nov. 1, 2007), available at www.ag.ny.gov (alleging that large national lender demanded that appraisers inflate property values).

My office, like others across the country, has worked with countless homeowners facing foreclosure as the result of these schemes. One of my first clients were an elderly couple from Parkersburg, West Virginia. Mr. F., a glass glazer, built their home himself in the evenings after work in the 1980s. In 2002, the Fs had a fixed rate mortgage, which a loan officer began aggressively soliciting them by phone for a refinance. After multiple calls and promises, the Fs broke down and applied for the loan. The lender then directly contacted an appraiser who it regularly secured inflated valuations from. Although the Fs' home was actually only worth $50,000, the appraiser provided a value of nearly $100,000. Even though they did not ask for it, the loan was increased to the full appraised value. Instead of what they'd been promised, the Fs' payments increased, their interest rate increased, their home secured debt obligation increased, and they were switched from a fixed to an adjustable rate mortgage. I met the Fs after their payments skyrocketed and they had no way to refinance the loan or save the home they had built. I have countless examples like these of lenders who knew exactly which appraisers to contact to provide inflated loans that led inexorably to foreclosure.

Another client was Mrs. R, a single, middle-aged woman. Mrs. R was repeatedly solicited to refinance her loan in the early 2000s. After purchasing her home for $15,000 in the mid-1990s, Mrs. R fell prey to a mortgage broker-appraiser team, who soon had her in a loan exceeding $70,000. Scared of losing her home and looking for lower payments, Mrs. R entered her information into a website that advertised that it could lower her bills. Soon an out-of-state lender contacted her and promised lower payments. This lender did not bother with an appraisal from a licensed appraiser; instead, it utilized an automated valuation model (AVM) of her home which provided a wholly inaccurate and inflated valuation of her home based on faulty market data. Although her home was actually only worth $34,000, the lender told her that her home was worth $84,000 based on the AVM. The lender pressured her to borrow additional funds up to the "value" of her home to pay other debts. I met Mrs. R. when the interest only feature of her loan expired and she was faced with impossibly high payments. Mrs. R. tried to refinance, but she was rejected because the loan so far exceeded the value of her home. Now she faced foreclosure.

Mrs. R's situation highlights the need for appraisals conducted by properly educated and regulated appraisers, rather than alternative methods. The automated valuation used by her lender was based on aggregate data from unverified public records that is often inaccurate, incomplete, or outdated. Moreover, programs like these cannot adequately consider neighborhood, condition of the property, location appeal, or altered building characteristics. Each of these factors is essential in understanding the true value of a home.

Incentives for Appraisal Fraud

Without the strict requirements imposed by the Dodd Frank Act, the financial incentives of those involved in the mortgage loan process work against honest appraisals.[18] Origination fees

[18] *See* Wallace v. Midwest Fin. & Mortg. Services, Inc., 714 F.3d 414, 422 (6th Cir. 2013) (reversing summary judgment in favor of creditor on civil racketeering claim; noting that lender not dissuaded by facially unreasonable appraisal); Fed. Hous. Fin. Auth. v. JPMorgan Chase & Co., 902 F. Supp. 2d 476 (S.D.N.Y. 2012) (quoting amended complaint, "WaMu falsely overstated appraisals in order to secure low LTV ratios for mortgages, thereby making the loans more attractive to prospective purchasers of certificates"); David Callahan, Home Insecurity: How Widespread Appraisal Fraud Puts Homeowners at Risk (Mar. 2005), available at www.demos.org.

for lenders and loan brokers are commonly based on the amount of the mortgage loan.[19] This can make lenders and brokers complicit in, or simply indifferent to, appraisal fraud because higher loan volume and higher loan amounts lead to greater profits.[20] Some lenders may deliberately seek inflated appraisals in order to trap borrowers in abusive loans and prevent them from refinancing.[21] Lenders' indifference to appraisal fraud may be traceable, at least in part, to securitization, which allows them to pass on the risk of loss while retaining minimal liability in the event of default by the borrower.[22] Lenders also rely on mortgage insurance to insulate them either partially (or fully, in the case of the government-backed FHA insurance), from the risk of loss after foreclosure. Secondary market participants, those who buy loans from lax lenders, can also purchase their own

[19] *Cf.* 15 U.S.C. § 1639b(c)(1) (explicitly permitting compensation for loan originators to be based on loan amount).
[20] *See* Fed. Hous. Fin. Auth. v. JPMorgan Chase & Co., 902 F. Supp. 2d 476 (S.D.N.Y. 2012) (quoting amended complaint, "WaMu falsely overstated appraisals in order to secure low LTV ratios for mortgages, thereby making the loans more attractive to prospective purchasers of certificates"); In re Bear Stearns Mortg. Pass-Through Certificates Litig., 851 F. Supp. 2d 746 (S.D.N.Y. 2012) ("[L]oan officers applied 'intense' pressure on underwriters to approve risky loans and rewarded 'high producers.'"); Cedeno v. IndyMac Bancorp, Inc., 2008 WL 3992304 (S.D.N.Y. Aug. 26, 2008) (alleging that lender selected appraisers, who provided inflated appraisals, in order to complete more transactions and earn greater profits; granting lender's motion to dismiss RESPA and TILA claims). *Cf.* United States v. Grintjes, 237 F.3d 876 (7th Cir. 2001) (discussing evidence that tended to show that mortgage broker had knowledge of clients' property flipping scheme); Am. Mortg. Network v. Shelton, 2006 WL 909415 (W.D.N.C. Apr. 6, 2006) (discussing how a buyer arranged for and helped prepare a fraudulent appraisal), aff'd, 486 F.3d 815 (4th Cir. 2007).
[21] *See, e.g.,* Tocco v. Argent Mortg. Co., 2007 WL 170855 (E.D. Mich. Jan. 18, 2007) (describing a borrower's inability to refinance an Argent loan when the appraisal for the refinancing came in $300,000 lower than the appraisal, performed less than a year previously, on which the original loan had been based); Office of the New York State Att'y Gen., Press Release, N.Y. Attorney General Sues First American and Its Subsidiary for Conspiring with Washington Mutual to Inflate Real Estate Appraisals (Nov. 1, 2007), available at www.ag.ny.gov (alleging that large national lender demanded that appraisers inflate property values).
[22] *See, e.g.,* Wallace v. Midwest Fin. & Mortg. Services, Inc., 714 F.3d 414, 422 (6th Cir. 2013); Homeward Residential, Inc. v. Sand Canyon Corp., 2014 WL 2510809, at *9–10 (S.D.N.Y. May 28, 2014) (refusing to dismiss trust's breach of warranty claims against Option One based upon appraisal fraud); Prudential Ins. Co. v. Credit Suisse Sec. (USA) L.L.C., 2013 WL 5467093 (D.N.J. Sept. 30, 2013) (investor suit against parties to a securitization of New Century and Option One loans; fraud claim based on pattern of false appraisals survived motion to dismiss); Fed. Hous. Fin. Auth. v. JPMorgan Chase & Co., 902 F. Supp. 2d 476 (S.D.N.Y. 2012); Fed. Hous. Fin. Agency v. UBS Americas, Inc., 858 F. Supp. 2d 306, 320 (S.D.N.Y. 2012), aff'd, 712 F.3d 136 (2d Cir. 2013); HSH Nordbank AG v. Barclays Bank PLC, 986 N.Y.S.2d 866, 2014 WL 841289, at *15, 18 (Sup. Ct. 2014) (table) (refusing to dismiss investor claims of fraud against seller and depositor in deal involving Fremont Inv. & Loan and New Century Mortg. Co. loans based on appraisal fraud; data showed approximately 24.5%–51.6% of the loans had combined loan-to-value ratios of over 100%, which contradicted the offering documents). *See also* Settlement Agreement, Annex 1, Statement of Facts at 4–5, U.S. Dep't of Justice & JPMorgan Chase & Co. (Nov. 19, 2013), available at www.justice.gov (describing JPMorgan's purchase and pooling into securities of loans it knew were missing appraisals, its tolerance for appraisals of 15% below loan amount, even when the loan-to-value ratio was 100%, and its inclusion in securitizations of loans that exceeded even that tolerance).

Secondary market purchasers may not be vigilant in policing lenders because they underestimate the risk of inflated appraisals or because they may be insured against this kind of fraud. See, e.g., Mass. Mut. Life Ins. Co. v. Residential Funding Co., 843 F. Supp. 2d 191 (D. Mass. 2012) (securities disclosures insufficient to put secondary market purchaser on notice that appraisers were systematically abandoning the represented appraisal procedures). In these cases, the insurer bears the risk of loss instead of the trust or other secondary market purchaser.

Some of the notorious FAMCO loan trusts were insured by mortgage guaranty policies issued by MBIA Insurance Corp. Stipulation of Settlement, Fed. Trade Comm'n v. First Alliance Mortg. Co. (In re First Alliance Mortg. Co.), No. SA CV 00-964 (C.D. Cal. Feb. 25, 2002), available at www.ftc.gov.

insurance against failure and so have reduced incentives to police the pool,[23] even if the disclosures are enough to put them on notice of the inflated appraisals.[24]

In some cases, appraisers received direct benefits for their participation in the fraud, through the promise of repeat business or more overt kickbacks or payment schemes.[25] Other times, lenders and brokers pressure appraisers to hit or exceed a predetermined value.[26] Failure to do so could lead the lender or broker to withhold business from the appraiser, to refuse to pay the appraiser, or to blacklist the appraiser.[27]

Appraisers themselves advocated for tighter regulation to protect their industry. In 2007, a petition with 11,000 appraiser signatures was delivered to Washington explaining that "Lenders . . . as a normal course of business, apply pressure on appraisers to hit or exceed a predetermined value. . . . We believe that this practice has adverse effects on our local and national economies and that the potential for great financial loss exists. We also believe that many individuals have been adversely affected by the purchase of homes which have been over-valued."[28] The appraisers went on to request that the government appropriately regulate the market to protect appraisers from "pressur[e] . . . to do dishonest appraisals."[29] Given the potential incentives for lenders and appraisers to inflate appraisal amounts, the need for focused oversight and effective supervision of both appraisers and appraisal practices has long been recognized.[30]

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[23] *See, e.g.,* Stipulation of Settlement, Fed. Trade Comm'n v. First Alliance Mortg. Co. (In re First Alliance Mortg. Co.), No. SA CV 00-964 (C.D. Cal. Feb. 25, 2002), available at www.ftc.gov (noting insurance of some of the notorious FAMCO loan trusts by mortgage guaranty policies issued by MBIA Insurance Corp.).

[24] *See, e.g.,* Mass. Mut. Life Ins. Co. v. Residential Funding Co., 843 F. Supp. 2d 191 (D. Mass. 2012) (securities disclosures insufficient to put secondary market purchaser on notice that appraisers were systematically abandoning the represented appraisal procedures).

[25] *See* First Magnus Fin. Corp. v. Star Equity Funding, L.L.C., 2007 WL 414272 (D. Kan. Feb. 2, 2007) (discussing scheme between mortgage brokers and appraisers).

[26] *See, e.g.,* Wallace v. Midwest Fin. & Mortg. Services, Inc., 714 F.3d 414, 417 (6th Cir. 2013) (describing scheme whereby broker requested appraisal value needed from the appraiser); Davis v. Wells Fargo Bank, 976 F. Supp. 2d 870, 876 (S.D. Tex. 2013) (describing pressure brought to bear on appraisers to produce low values at foreclosure sales of property, allegedly in order to maximize paper losses for tax purposes), dismissed on other grounds, 2014 WL 585403 (S.D. Tex. Feb. 14, 2014); Office of the New York State Att'y Gen., Press Release, N.Y. Attorney General Sues First American and Its Subsidiary for Conspiring with Washington Mutual to Inflate Real Estate Appraisals (Nov. 1, 2007), available at www.ag.ny.gov (detailing scheme in which a large national lender demanded that appraisers inflate property values).

[27] *See* Davis v. Wells Fargo Bank, 976 F. Supp. 2d 870, 876 (S.D. Tex. 2013) (appraiser who did not meet target values was blacklisted), dismissed on other grounds, 2014 WL 585403 (S.D. Tex. Feb. 14, 2014); Fed. Hous. Fin. Auth. v. JPMorgan Chase & Co., 902 F. Supp. 2d 476 (S.D.N.Y. 2012) (quoting amended complaint; "WaMu selected individual appraisers who were willing to produce false, inflated appraisals and refused to hire appraisers who maintained their independence."); Gaudie v. Potestivo Appraisal Services, 837 F. Supp. 2d 799 (N.D. Ill. 2011) (discussing appraiser's possible motivation in inflating appraisal, noting that the appraiser was dependent on lender for employment and "had to give [it] the the appraised values [it] desired if [he] wanted to work in that field"); Office of Pol'y Dev. & Research, U.S. Dep't of Hous. & Urb. Dev., Report to Congress on the Root Causes of the Foreclosure Crisis 40–41 (2010), available at www.huduser.org (arguing that appraisal fraud depends on lack of underwriting control of the broker and appraiser). See also People v. First Am. Corp., 878 N.Y.S.2d 860 (Sup. Ct. 2009) (recounting complaint's allegations of lender control of appraisers, in violation of state law and Uniform Standards of Professional Appraisal Practice), aff'd, 902 N.Y.S.2d 521 (App. Div. 2010).

[28] Appraisers Petition, available at http://appraiserspetition.com.

[29] *Id.*

[30] Office of Pol'y Dev. & Research, U.S. Dep't of Hous. & Urb. Dev., Report to Congress on the Root Causes of the Foreclosure Crisis 40–41 (2010), available at www.huduser.org (arguing that appraisal fraud depends on lack of

Consequences of Appraisal Fraud

The consequences of appraisal fraud are far reaching.[31] When a borrower becomes bound to a mortgage that exceeds the value of his home at origination, he is immediately prohibited from refinancing to obtain better loan terms, such as a fixed interest rate or lower interest rate. Unlike with other types of loans, this is of significant import because the borrower's home is placed at risk. Moreover, predatory lenders often pair overvalue mortgages with other exploitative terms that make a borrower's need to refinance even more pressing.[32] In addition, the borrower cannot sell his home to relocate, even if he needs to do so to find work.[33] And when the borrower finds himself in this dire situation, the last resort protections provided by the bankruptcy code provide him with little assistance. Even if he chooses to declare bankruptcy, the homeowner must pay the full balance of the mortgage or forfeit his home; he cannot avail himself of the relief available for unsecured debts or debts secured by personal property, which can be discharged or reduced to the value of the collateral.[34] The homeowner becomes trapped with no way out of the loan except foreclosure. Finally, unlike with other loans, realizing on the security interest for a home-secured loan can result in homelessness, a far greater impact than loss of personal goods or loss of credit, and has negative spillover onto the surrounding community.[35]

Indeed, for many of these reasons, placing a borrower underwater significantly increases the risk of foreclosure.[36] Empirical data demonstrates that higher loan to value ratios lead to an increased risk of foreclosure. For example, securities ratings agencies have determined that loans with LTV ratios between 95% and 100% are 4.5 times more likely to enter foreclosure than loans with ratios below 80%. Loans that exceed 100% of the market value of the collateral are even more likely to enter foreclosure.[37] As a HUD-Treasury Report during the Bush Administration explained,

> Many of the borrowers who are victims of this [fraudulent appraisal] scheme cannot afford to repay or refinance the mortgage based on the inflated price, and these loans may go into default and foreclosure quickly. Appraisers and others engaging

underwriting control of the broker and appraiser). *See, e.g.*, Fed. Reserve Bank of Atlanta, Appraisal Reviews Are Important to Safe Banking, Fin. Update, 4th Quarter, 2004, available at www.frbatlanta.org.

[31] As the Sixth Circuit noted, "a borrower has much to lose from entering into a too-big loan." Wallace v. Midwest Fin. & Mortg. Services, Inc., 714 F.3d 414, 422 (6th Cir. 2013).

[32] *See, e.g., id.* at 421 (noting key role of inflated appraisal in inducing borrower to take out overpriced payment-option ARM, with high fees and "unreasonable" terms, resulting ultimately in borrower's loss of home and bankruptcy).

[33] The public policy against such transactions tracks the longstanding public policy against restraints on landowners that limit their ability to transfer or otherwise control their real property. *See, e.g.*, *McCreery v. Johnston*, 110 S.E. 464, 466 (W. Va. 1922).

[34] *See* 11 U.S.C. §§ 521(a)(2)(A), 1322(b)(2).

[35] *See* Adam J. Levitin & Tara Twomey, *Mortgage Servicing*, 28 Yale J. on Reg. 1, 69 (2011); David Callahan, *Home Insecurity: How Widespread Appraisal Fraud Puts Homeowners at Risk* (Mar. 2005), *available at* www.demos.org/sites/default/files/publications/home_insecurity_v3.pdf.

[36] Laurie S. Goodman et al., *Negative Equity Trumps Unemployment in Predicting Defaults*, 19 J. Fixed Income 67 (2010).

[37] See Federal Housing Finance Agency v. Nomure Holding America, Inc., 104 F.Supp.3d 441, 465 (S.D.N.Y. 2015).

> in this fraudulent practice are helping to send first-time home buyers and whole communities into economic ruin.[38]

While homeowners feel the direct impact of these foreclosures, investors, insurers, neighboring homeowners, and ultimately taxpayers incur significant losses from foreclosures caused by appraisal fraud.

Regulation

FIRREA

In 1989, Congress, in response to the savings and loan crisis of the 1980s, enacted the Financial Institutions, Recovery, Reform, and Enforcement Act of 1989 (FIRREA).[39] Under FIRREA, Congress mandated appraisal standards, review of appraisals and supervision of appraisers by lenders, and appraiser independence. FIRREA has the express purposes of ensuring that:

> Federal financial and public policy interests in real estate related transactions will be protected by requiring that real estate appraisals utilized in connection with federally related transactions are performed . . . by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision.[40]

Guidelines promulgated by the federal banking agencies under FIRREA require covered institutions to establish an effective real estate and evaluation program that, among other things, ensures appraiser independence, provides for adequate review of appraisals, and monitors appraisers and reviewers. Institutions are also directed to establish policies and procedures for resolving any inaccuracies or weaknesses in an appraisal prior to the credit decision.[41]

As part of FIRREA,[42] in order to ensure that appraisals were conducted according to "uniform standards,"[43] Congress required that each federal banking regulator adopt rules governing appraisal standards, including the promulgation of appraisal standards and appraisal reviews for compliance with the Uniform Standards of Professional Appraisal Practice (USPAP).[44] Among other things, the rules of conduct state that an appraiser may not accept a fee for an assignment that is contingent upon the reporting of a predetermined result or of a particular amount of the value opinion.[45]

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[38] *See* HUD-Treasury National Predatory Lending Task Force, Joint Report: Curbing Predatory Home Mortgage Lending (2000), *available at* http://archives.hud.gov/reports/treasrpt.pdf.
[39] Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183; H. Rep. No. 101-54(I), at 311, reprinted in 1989 U.S.C.C.A.N. 86 (discussing role of faulty appraisals in the crisis).
[40] 12 U.S.C. § 3331.
[41] 75 Fed. Reg. 77,450, 77,463 (Dec. 10, 2010).
[42] Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183.
[43] 12 U.S.C. § 3331.
[44] Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, tit. XI, § 1110, 103 Stat. 183 (as codified at 12 U.S.C. § 3339).
[45] 2016-2017 USPAP at 8-9, available at www.appraisalfoundation.org.

Truth in Lending Act

Regulations issued under the Truth in Lending Act set some additional requirements for appraisals done in connection with higher-priced mortgage loans,[46] including that the appraisal be completed by a licensed appraiser who conducts a physical inspection of the interior of the home.[47] If the loan is a purchase-money loan, the property was purchased by the seller within the previous six months, and the new purchase price exceeds the old by certain amounts, the lender is responsible for getting two written appraisals.[48]

Dodd-Frank Act

Additionally, regulations promulgated in the Truth in Lending Act, pursuant to the Dodd-Frank Act, regulate the supervision of appraisers.[49] Lenders are prohibited from extending credit when they know that an appraisal materially misrepresents the value of the consumer's principal dwelling. Creditors may only escape liability if they exercised "reasonable diligence."[50] Creditors and settlement service providers are required to report any material failure to follow USPAP by an appraiser.[51]

Appraiser Independence

Standards for appraisals and review of appraisals are not, by themselves, enough to prevent coercion of appraisers by lenders and brokers anxious to make the deal. Independence is a key component of protecting the market from the widespread overvaluation that triggered the savings and loan crisis in the 1980s and the subprime collapse in the 2000s. Since 1989, federal law has attempted to protect appraisers by forbidding lenders from offering anything of value in exchange for an appraisal performed by other than a certified or licensed appraiser.[52] In 2008, the Federal Reserve Board used its authority to prohibit unfair or deceptive acts and practices to prohibit creditors, mortgage brokers, and their affiliates from exercising inappropriate influence over the amount at which a consumer's home is appraised.[53] Fannie Mae and Freddie Mac have both issued

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[46] *See* National Consumer Law Center, Truth in Lending §§ 9.5.2, 9.5.4 (9th ed. 2015), updated at www.nclc.org/library (discussing the definition of higher-priced mortgage loans for purposes of the appraisal rules).
[47] National Consumer Law Center, Truth in Lending § 9.5.4.6 (9th ed. 2015), updated at www.nclc.org/library (discussing the appraisal regulations for higher-priced mortgage loans).
[48] 12 C.F.R. § 1026.35(c)(4) (eff. Jan. 18, 2014). See generally National Consumer Law Center, Truth in Lending § 9.5.4.6 (9th ed. 2015), updated at www.nclc.org/library (discussing the appraisal regulations for higher-priced mortgage loans).
[49] *See generally* National Consumer Law Center, Truth in Lending §§ 9.4.2 (discussing the appraisal regulations issued under Truth in Lending Act), 9.4.4 (reviewing Truth in Lending Act remedies for violations of these regulations) (9th ed. 2015), updated at www.nclc.org/library.
[50] 12 C.F.R. § 1026.42(e).
[51] 12 C.F.R. § 1026.42(g)(1). *See generally* National Consumer Law Center, Truth in Lending §§ 9.4.2 (discussing the appraisal regulations issued under Truth in Lending Act), 9.4.4 (reviewing Truth in Lending Act remedies for violations of these regulations) (9th ed. 2015), updated at www.nclc.org/library.
[52] 12 U.S.C. § 3349(a)(1).
[53] 12 C.F.R. § 1026.42.

guidance specifically addressed to the question of appraiser independence.[54] Bolstering the independence of appraisers and sheltering them from lender coercion has been at the heart of actions taken by the New York attorney general (in negotiating the settlement of an appraisal fraud investigation)[55] and regulations issued under the Dodd-Frank Act.[56]

Regulations promulgated under the Dodd-Frank Act's amendments to the Truth in Lending Act have prohibited the falsification or alteration of an appraisal and a number of coercive practices that might influence an appraiser's valuation.[57] In addition, the regulations limit conflicts of interest and require reasonable compensation of appraisers.[58] The Dodd-Frank Act also included provisions regarding licensure of appraisers and appraisal management companies.[59]

Impact of Regulation & Discussion Topics

These reforms have worked. Unethical lenders, brokers, and appraisers can no longer join forces to defraud homeowners, communities, investors, and insurers. Appraisal independence is the cornerstone of this regime. These requirements build upon earlier steps taken under FIRREA to ensure minimum standards for appraisals and appropriate training. The requirement of a complete appraisal by a licensed and educated appraiser further protects the market.

The home buying and refinancing process is not currently complicated or difficult, and minimum regulatory requirements are necessary to protect homeowners and the economy at large. Any appraiser shortage would be appropriately addressed through market forces: increased demand would lead to increased customary rates, which would accordingly lead to a greater supply of appraisers entering the marketplace. Moreover, any shortage is likely to be temporary and to disappear as interest rates increase and the demand for mortgage refinances decreases. Lowering standards and qualifications, including permitting lenders to rely on alternative valuation products and broker price opinions, will further increase any such shortage, rather than remedy the need for qualified appraisers. Such reliance would further enable lenders to return to obtaining unreliable reports which, in turn, create instability in the market. In short, the regulatory regime is a floor that is essential to avoid both unintentional errors as well as fraud.

Indeed, lowering the *de minimis* appraisal threshold for Federally Related Transactions would assist in addressing any appraiser shortage. More importantly, lowering this threshold—which currently only requires an appraisal for loans over $250,000 or for Higher Priced Mortgage Loans over $25,000—would protect homeowners and communities. The majority of homes

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[54] Fannie Mae, Appraiser Independence Requirements (Nov. 10, 2010), available at www.efanniemae.com; Freddie Mac, Oct. 15 Guide Bulletin 2010-23, available at www.freddiemac.com.

[55] Office of the New York State Att'y Gen., Press Release, New York Attorney General Cuomo Announces Agreement with Fannie Mae, Freddie Mac, and OFHEO (Mar. 3, 2008), available at www.ag.ny.gov.

[56] Pub. L. No. 111-203, §§ 1472, 1473, 124 Stat. 1376 (2010); 75 Fed. Reg. 66,554 (Oct. 28, 2010). See 12 C.F.R. § 1026.42; National Consumer Law Center, Truth in Lending § 9.4.2.1 (9th ed. 2015), updated at www.nclc.org/library) (replacement of Federal Reserve Board's 2008 appraisal rules and effective dates).

[57] *See* 12 C.F.R. § 1026.42; National Consumer Law Center, Truth in Lending § 9.4.2.1 (9th ed. 2015), updated at www.nclc.org/library (replacement of Federal Reserve Board's 2008 appraisal rules and effective dates).

[58] *See* National Consumer Law Center, Truth in Lending §§ 9.4.2.3–9.4.2.5 (9th ed. 2015), updated at www.nclc.org/library (substantive prohibition of appraisal regulation).

[59] Pub. L. No. 111-203, § 1473, 124 Stat. 1376 (2010).

throughout the country are worth less than $250,000.[60] Low- and moderate-income homeowners—and the government entities that insure or invest in their loans—deserve the same protections as higher income homebuyers.

A floor of overarching federal regulatory standards for lending and appraisals is necessary to ensure that both consumers and others impacted by the mortgage market are uniformly protected from fraud nationwide. National standards are appropriate for a national market in mortgage lending, investment, and insurance; and to enable appraisers to more easily act with reciprocity in jurisdictions and across state lines, where appropriate. Without this uniform baseline, the marketplace would become more costly and complicated for participants. Both the savings and loan crisis of the 1980s and the mortgage industry collapse in the 2000s demonstrate the clear and pressing need for this federal regulatory framework to establish a floor for acceptable appraisal conduct. Eliminating these protections and relying solely on the states would open the door to more economic crises that devastate homeowners and financial institutions alike. Of course, these federal protections are, appropriately, a floor and not a ceiling on appraisal safeguards. States have always been and continue to be able to create additional, state appropriate protections. This interplay between basic protections on a federal level with *additional* localized regulation is necessary and positive for the market and consumers.

Conclusion

In sum, it is essential that a national regulatory floor be retained and built upon to protect the American dream of homeownership into the future. Without these protections, the market will become more costly in the short term, and lead to new financial crises in the future, even while we have barely recovered from the last one. The appraisal protections were wisely adopted by Congress in response to real, demonstrated need in the very recent past. I urge you to keep these essential protections in place.

[60] *See* S&P Dow Jones Indices LLC, S&P/Case-Shiller 20-City Composite Home Price Index© [SPCS20RSA], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/SPCS20RSA, November 13, 2016.

PO Box 5613
Greensboro, NC 27435

April 29, 2015

Over the past year, a select group of professional appraisal organizations have met to discuss what are jointly viewed as major problems facing our appraisal profession. The results of these discussions are outlined below and in the accompanying document entitled ***Regulatory Issues Affecting the Real Estate Appraisal Profession.***

Real estate appraisers are currently experiencing significant pressures that threaten the structure and integrity of the appraisal profession while posing financial risks to consumers. We believe that the declining attractiveness of the appraisal profession to new entrants is a major problem, leading to a dwindling qualified appraiser population, lack of transparency in the appraisal process as underwriters off-load risk, and consumers being offered fewer and lower quality professional tools related to one of their most significant financial investments for which they are required to arrive at a fully informed, intelligent decision.

We, the undersigned professional appraisal organizations, seek the following actions to help stabilize the market for practitioners and consumers (taxpayers) alike:

1. Create a more effective training structure to support Appraiser Trainees in order to support and promote growth in the appraisal profession.
2. Improve transparency in the valuation process by:
   a. Enforcing consistency in state licensing requirements.
   b. Supporting mandatory licensing rules that require the use of licensed or certified appraisers for any services for which an opinion of value for real property is developed.
   c. Requiring complete disclosure and breakdown of the components covered by the appraisal fees.
3. Lower the de minimis threshold from $250,000 TO $25,000, providing consumers, at all levels, the opportunity to benefit in their decision making process by providing a professional, unbiased opinion of value.
4. Enforce payment of "customary and reasonable" fees to appraisers to protect the profession against declining fees and the assumed related decline in appraisal quality.
5. Encourage heightened appraisal scrutiny of all loan types including Qualified Mortgages and government-sponsored entities (GSE) by amending regulations to ensure that lenders are held to the same standards as that required of higher-risk mortgages.
6. Relax the three-day requirement for appraisal fee estimates by lenders to allow them sufficient time to estimate these fees given the potential complexities of appraisals versus other required criteria, such as routine credit reports, flood certifications, and tax services.
7. Support additional consumer access to educational products relating to the appraisal process.

The attached summary describes each of the actions listed above along with suggested solutions. In addition, a more detailed analysis including the historical development of the issues is available at http://www.columbiasociety.org.

We are very interested in discussing this issue with you or representatives from your office. Please contact us at 800-827-2720 to discuss and/or arrange for a date to meet so that we may discuss in person.

Respectfully,

American Society of Appraisers
Columbia Society of Real Estate Appraisers
Instituto de Valuadores de Puerto Rico
Massachusetts Board of Real Estate Appraisers
National Association of Independent Fee Appraisers
North Carolina Professional Appraisers Coalition

The professional appraisal organizations shown above are all proud sponsors of The Appraisal Foundation.

American Society of Appraisers appraisers.org **Signed by: James R. Hirt** James R. Hirt **Title: Chief Executive Officer** **American Society of Appraisers**	MBREA Massachusetts Board of Real Estate Appraisers mbrea.org **Signed by: Stephen E. Sousa** **Title: Executive Vice President** **Massachusetts Board of Real Estate Appraisers**
Columbia Society of Real Estate Appraisers Education is the Key to Success Columbia Society of Real Estate Appraisers columbiasociety.org **Signed by: William H. Green III** William H. Green III **Title: National President** **Columbia Society of Real Estate Appraisers**	NAIFA National Association of Independent Fee Appraisers naifa.com **Signed by: Nina W. Henderson** Nina W. Henderson, IFA **Title: President** **National Association of Independent Fee Appraisers**
INSTITUTO DE EVALUADORES DE PUERTO RICO Instituto de Evaluadores de Puerto Rico iepr.net **Signed by: Gilberto Santana** Gilberto Santana **Title: President** **Instituto de Valuadores de Puerto Rico**	North Carolina Professional Appraisers Coalition ncpac.org **Signed by: Christie L. Standish** Christie L. Standish **Title: President** **North Carolina Professional Appraisers Coalition**

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REGULATORY ISSUES FACING THE REAL ESTATE APPRAISAL PROFESSION

Unintended Consequences of the Dodd-Frank Law and Potential Remedies

Summary Document

Regulatory Issues Facing the Real Estate Appraisal Profession

Executive Summary

The real estate appraisal profession has experienced massive changes in recent years. The fallout from the Subprime Mortgage/Financial Crisis of 2007-2008 and the Dodd-Frank legislation that followed left the profession in disarray. Though the intention of Dodd-Frank was, in part, to protect the independence of the appraiser, it has done little to accomplish that goal. The purpose of this paper is to highlight significant issues facing the real estate appraisal profession and present potential solutions to the issues. Although the paper is focused on issues in the residential profession, we recognize that many of these problems could also affect other categories of appraisal.

This document addresses only the main problems as perceived by the appraisal profession and our proposals for addressing those issues to the benefit of consumers and the profession as a whole. A more detailed white paper has been prepared by this group that provides a wider view of the historical aspects that underpin current conditions in the appraisal profession and the impact these conditions have on consumers. We would strongly urge the reader to refer to that document in conjunction with these recommendations.

Regulatory Issues Facing the Real Estate Appraisal Profession

There needs to be recognition of the dwindling appraiser population, and steps must be taken to encourage entry into the appraisal profession

According to data available from the United States Census Bureau and published in an April 2013 article by the Appraisal Institute, the number of appraisers nationwide peaked in 2007 at 118,657. The ASC lists the current number of appraisers at 100,129 as of April 2015. Although these statistics represent total credentials rather than the actual number of appraisers (i.e. an appraiser may be counted multiple times if he/she is credentialed in multiple states), the trend is clear; a decline in appraiser credentials of more than 15% over the 6-plus year period.

The decline is due in part to age attrition and fewer new entrants into the field. Another reason cited for the drop in appraiser credentials is increased use of alternative valuation products and/or broker price opinions (BPOs) by lenders. These factors, coupled with overall challenging business conditions and convoluted new government regulations, have led to limited growth opportunities in the real estate appraisal profession.

Throughout this paper we will explore various factors that have influenced the decline in credentials; and we will give recommendations of how to improve the attractiveness of the profession to new entrants while protecting consumers.

1. The appraisal profession and users of professional appraiser services must create an environment that encourages Appraiser Trainees

In today's market for federally related transactions, lenders and AMCs do not typically accept work from anyone other than licensed or certified appraisers. This practice leaves appraisal trainees with no way to earn the work experience required by law. This structure discourages established appraisers from hiring Appraiser Trainees. The profession must take on the responsibility for training new entrants; otherwise, there will be too few appraisers remaining to assume responsibility from those retiring.

Recommendation:
The Appraisal Qualifications Board (AQB) currently has in place qualification criteria for Appraiser Trainees that gives clear guidelines for trainees and the supervisory appraisers who oversee them. Quality training programs need to be designed and implemented to support and link the educational and experience requirements for appraising.

In one model, appraisal students could spend two years of a 4-year program dedicated to learning general and appraisal-specific concepts, followed by two years of a combined education/work experience program, thus allowing students to graduate with the qualifications for becoming certified appraisers.

Regulatory Issues Facing the Real Estate Appraisal Profession

We feel that it is important to also encourage lenders and AMCs to adopt policies regarding trainees and supervising appraisers and not insist that trainees be accompanied on inspections beyond the point where they are considered competent by their supervising appraisers.

2. Consumers would benefit from added transparency in the valuation process

Lack of consistency in state licensing requirements leaves consumers vulnerable to comparability and reliability issues. Presently, only 37 licensing jurisdictions require mandatory licensing, and the rest are either voluntary or mandatory for federally related transactions only. Another issue associated with transparency is the lack of disclosure about the components covered by the appraisal fees, such as lender fees, fees paid for AMC services, and direct appraisal fees.

Recommendation:
We propose mandatory licensing rules be put in place and enforced in all states, requiring the use of licensed or certified appraisers for any services for which an opinion of value for real property is developed. Mandatory licensing in all states would improve the comparability and reliability of appraiser valuations nationwide, supporting consumer's need for better information during the home buying process. It is also our opinion that each component of the appraisal fee should be listed separately when disclosed to the client, so that consumers know fully where their money goes as part of the overall mortgage transaction.

3. The federal de minimis appraisal threshold should be reduced to encompass more valuation assignments

The de minimis appraisal threshold, the dollar level set by the federal financial regulators to exempt real estate loans made by federally insured financial institutions from statutory appraisal requirements, was increased in 1994 from $100,000 to $250,000 as a way to reduce regulatory burden and encourage economic growth. Though many groups have lobbied to reduce the de minimis since that time, none have been successful except in one type of mortgage loan, the Higher-Priced Mortgage Loans (HPML)[1].

It is important to note that in December 2012, the Federal Register discussed HPMLs and established a $25,000 de minimis for these loan types. In January 2013, after the Final Rule was issued, a consumer advocacy group expressed the view that "lower- to middle-income consumers needed the same protections as those seeking HPMLs."[2] When the final rule was issued, the de minimis for HPMLs was set at $25,000, or 1/10 that established for all other

[1] TILA Regulation Z defines HPML's as: "a consumer credit transaction secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 or more percentage points for loans secured by a first lien on a dwelling, or by 3.5 or more percentage points for loans secured by a subordinate lien on a dwelling."
[2] Federal Register, Vol. 78, No. 248, December 26, 2013. 78529.

federally related transactions. The de minimis for all other mortgage loans has remained at $250,000.

Data analyzed for this paper, taken from the S&P Case-Shiller 20-City Home Price Index for the period 2009-2015, indicate that the average price for homes in surveyed markets ranged between $140,000 and $175,000.[3] The data show that, at a minimum, most residential real estate transactions are below the de minimis, thereby nullifying the federal requirement for an appraisal. Thus, many consumers are effectively being denied the right to professional appraisals in a significant amount of mortgage transactions.

Recommendation:
We propose that the existing de minimis threshold of $250,000 for all federally related mortgage transactions be lowered to $25,000 HPML Appraisal Rule passed by the combined efforts of the Department of the Treasury, Board of Governors of the Federal Reserve System and the Bureau of Consumer Financial Protection. Reducing the de minimis threshold would increase the number of transactions requiring professional appraisals, giving more consumers access to more reliable valuations.

4. More must be done to enforce the customary and reasonable fee requirements established by Dodd-Frank

The level of fees paid to appraisers is clearly one of the most important issues facing the profession. Declining fees currently being paid by AMCs to appraisers have discouraged new entrants from coming into the profession.

One of the mandates of Dodd-Frank is the requirement for State appraiser certifying and licensing agencies to register and oversee AMCs. At least one state, Louisiana, has gone a step further in dealing with the *customary and reasonable* debate. In May, 2012, Louisiana passed its *Louisiana Appraisal Management Company Licensing and Regulation Act*. The law requires that AMCs "compensate appraisers at a rate that is *customary and reasonable* for appraisals in the market area of the property being appraised, consistent with the presumptions of compliance under federal law."[4]

To determine what constitutes *customary and reasonable* fees, Louisiana authorized a statewide survey done by the Southeastern Louisiana University Business Research Center. The survey focused on fees being paid by lenders, not AMCs, to determine *customary and reasonable* fees for specific assignments in specific areas. The survey also included appraiser input for comparison. The final results of the survey set the standard for customary rates in various regions of Louisiana.

[3] https://research.stlouisfed.org/fred2/series/SPCS20RSA
[4] http://www.reab.state.la.us/AMC_license_law.html

Although AMCs operating in Louisiana are not bound to the rates prescribed, they are required to provide extensive documentation on how the rate used was developed if audited.

Another suggestion has been to use the Veteran Administration's (VA) fee schedule as a guideline, as it fairly reflects, at a minimum, fees associated with the work involved in appraisal development and reporting, as well as time frame (7 to 10 days in most markets), and other requirements to develop and report credible and USPAP-compliant appraisals.

Recommendation:
We suggest that all states follow the Louisiana AMC law and begin regulating AMCs as Dodd-Frank mandates. Furthermore, states should follow the Louisiana model and conduct their own independent studies to determine what *customary and reasonable* fees should be for their geographic areas. Where studies have not yet been developed, we suggest the use of VA rates as an alternative.

5. Lenders should critically analyze the value and condition of the property as well as the borrower's ability to pay

New regulations enacted by the Consumer Financial Protection Bureau, entitled *Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z)* state that "The act (Appraisals for Higher-Priced Mortgage Loans {HPML) Act)) contains special appraisal requirements with respect to higher-risk mortgages".[5] The HPML regulations contain language regarding a $25,000 *de minimis* and include very specific appraisal standards for higher priced mortgage loans. It is troubling that The Qualified Mortgage regulations further state that the following are exempt from these appraisal requirements:

- Qualified Mortgages
- Higher priced mortgages with a debt-to-income ratio of 43 or less
- Loans with a higher debt to income ratio that are purchasable by the GSAs or insurable by FHA (this is presumably a temporary provision)

The above three exclusions effectively remove the preponderance of loans from any defined appraisal requirements.

Recommendation:
To protect the homebuyer and ultimately the taxpayer, we argue that lenders should critically analyze the value of the property, the condition of the property and the borrower's ability to repay the loan. Ideally, lenders would be held responsible for failed loans within a reasonable time period (e.g. five years). Furthermore, lenders and not the AMCs should be held accountable for ordering these appraisals. This approach will contribute to ensuring that low cost and fast turnaround are not the basis for choosing qualified appraisers.

[5] Bureau of Consumer Financial Protection, *Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z)*, January 10, 2013.

6. More is needed to educate consumers on the role of appraisers in the mortgage origination process

Though consumers have a vague understanding of the appraisal process, they do not understand that one of the appraiser's main roles in the loan process is to protect the consumer. Appraisers have been unjustifiably blamed for "killing the deal" if the value comes in too low to satisfy the loan requirements.

Recommendation:
There are numerous pamphlets and flyers that explain the appraisal process to consumers; however, they are not being distributed widely. While The Appraisal Foundation is working closely with a public relations firm to promote the profession, federal and state governments must also participate in this educational process; financial institutions should be required to disseminate this information when accepting loan applications; and professional appraisal organizations could also support consumer education with wider distribution of educational and informational materials.

7. Lenders need more flexibility in estimating appraisal fees

There has been a change in the interpretation of the three-day requirement for estimates by lenders as a part of a 2014 TILA-RESPA Integrated Disclosure Rule that has made it very difficult for the lenders to select the most qualified appraiser at a reasonable and customary fee.

It is not difficult to estimate the cost of services such as credit reports, flood certifications, tax services, etc. since they are fairly well standardized; however, that is not true of an appraisal. In most cases, location, complexity of the valuation and scope of work cannot be immediately determined. Nonetheless, in order to comply with the 2014 TILA-RESPA rules, lenders are forced to quickly obtain and guarantee a fee. Time simply does not allow either the lender or a management company to analyze and determine a reasonable and customary fee for work undertaken by the most competent and experienced appraiser in such a short amount of time.

Recommendation:
To solve this problem, lenders should be given more flexibility in estimating the appraisal fee within the three day period and not be held to such strict requirements pertaining to upward adjustments in the cost of the appraisal. Where a state has performed an appraisal fee study, lenders may be better situated to provide more accurate estimates; as such, it is imperative that states engage in fee studies not only for the benefit of appraisers, but for consumer confidence in the estimated fee.

Additional thoughts:

Appraisers and underwriters should be allowed and encouraged to communicate with one another directly

We believe that it is important that underwriters who are responsible for verifying credibility and USPAP compliance of appraisal reports be allowed and encouraged to communicate directly with the appraiser. This would eliminate much of the confusion and promote efficient time usage in the appraisal process by reducing the amount of information and questions passed through AMCs to either the underwriter or the appraiser. A more efficient process would benefit the consumer.

Conclusion

The real estate appraisal profession is currently experiencing several challenges affecting both appraisal professionals and consumers. We believe that the declining attractiveness of the appraisal profession to new entrants could be addressed by:

1. Creating a more effective training structure for Appraiser Trainees to perpetuate the appraisal profession and support growth in the number of professionals in the market
2. Lowering the de minimis threshold, thereby increasing the amount of work available for appraisers and providing consumers, at all levels, the opportunity to benefit in their decision making process by providing a professional, unbiased opinion of value
3. Enforcing payment of *customary and reasonable* fees to maintain a fair environment for appraisers while discouraging further declining appraisal quality

Additionally, we believe that consumers would ultimately benefit from:

1. Increased transparency with respect to the role an AMC plays in the appraisal process, including a breakout of fees paid to AMCs for this role
2. A lower de minimis threshold, covering more transactions and providing consumers with access to a valuable tool in determining risk
3. Access to consumer education and educational products relating to the appraisal process

REGULATORY ISSUES FACING THE REAL ESTATE APPRAISAL PROFESSION

Unintended Consequences of the Dodd-Frank Law and Potential Remedies

Full Document

Regulatory Issues Facing the Real Estate Appraisal Profession

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Regulatory Issues Facing the Real Estate Appraisal Profession

Part 1 – Introduction

The real estate appraisal profession, in recent years, has encountered massive changes. The fallout from the Subprime Mortgage/Financial Crisis of 2007-2008 and the Dodd-Frank legislation that followed have left the profession in disarray. Though the intention of Dodd-Frank was, in part, to protect the independence of the appraiser, it has done little to accomplish that goal. The purpose of this paper is to:

- Present a historical perspective of the relationship between real estate appraisers and the lending industry,
- Review federal rules and regulations affecting real estate appraisers,
- Determine the impact of federal rules and regulations on the real estate appraisal profession, and;
- Highlight specific issues facing the real estate appraisal profession and present potential solutions to these issues.

Part 2 – Historical Context of the Real Estate Appraisal Industry

Setting the Stage

Before the era of the 30-year mortgage, typical mortgage loans were based on terms which required 50% down, interest-only payments, five-year terms and balloon payments of the outstanding mortgage balances at the end of the loan terms. These terms insured the solvency of the lender's portfolio.

In 1934, the federal government passed the National Housing Act in an attempt to revitalize the nation's economy and jumpstart the housing market, both of which were suffering greatly due to the Great Depression. The National Housing Act created the Federal Housing Administration (FHA). FHA's original mission was to insure mortgages originated by depository institutions; however, because lenders were required to hold these mortgages for the entire term of the loan, many institutions were reluctant to issue FHA loans.

In 1938, Congress created the Federal National Mortgage Association (FNMA – commonly known as Fannie Mae), which purchased mortgages from lenders, thus freeing up money the lenders could then relend to other borrowers. Along with Fannie Mae came more fair and efficient mortgage-lending practices. Now that lenders were going to a central funding source, loan terms, interest rates and underwriting guidelines began to be similar from institution to institution. Lenders had to conform to Fannie Mae's guidelines and restrictions if they wanted to sell their loans in the secondary market. In 1944, the Veterans Administration (VA) followed suit with a similar program for veterans and military personnel, who as a result could buy homes without down payments. This action catapulted the housing market.

Regulatory Issues Facing the Real Estate Appraisal Profession

In the 1950s, 60s and early 70s, most mortgages were 20-30 years loans. In 1968, FNMA was split into the current FNMA (Fannie Mae) and Government National Mortgage Association (GNMA), commonly known as Ginnie Mae. The present-day Fannie Mae is not a government agency, but a federally-chartered corporation owned by private shareholders. The present-day Fannie Mae purchases FHA, VA and conventional mortgages. The present-day Ginnie Mae is a government agency that does not purchase loans, but instead guarantees returns to investors who purchase mortgage-backed securities backed by FHA, VA and other government loans.

Baby boomers, both men and women, entered the workforce in the late 1960s and early 70s, creating double-income families. Boomers wanted larger, more expensive homes to fit their incomes and lifestyles. More mortgages were needed. In 1970, Congress chartered the Federal Home Loan Mortgage Corporation (FHLMC), better known as Freddie Mac, to increase the supply of mortgage funds available to commercial lenders, savings and loan institutions, credit unions and other mortgage lenders.

From the 1930s through the mid-70s, lenders (including thrifts) and residential real estate appraisers shared close working relationships. Lenders relied on the appraiser's knowledge and also his/her reputation. Lenders looked for appraisers who had affiliations with major nonprofit appraisal organizations in the selection process. There were many professional appraisal organizations, including The American Society of Farm Managers and Rural Appraisers – 1929 (AFMRA), The American Institute of Real Estate Appraisers - 1932 (AIREA), the Society of Real Estate Appraisers – 1935 (SRA), the American Society of Technical Appraisers – 1936 (AMSTA), the Technical Valuation Society – 1935 (TVS), the National Association of Independent Fee Appraisers – 1961 (NAIFA), and many others. The AMSTA and TVS merged in 1952 to become The American Society of Appraisers, and the AIREA and SRA merged in 1990 to form the Appraisal Institute. All of these professional organizations were formed to promote education and ethical standards as well as to attract competent appraisers.

Up to the mid-70s, mortgage requirements were generally understood by the average consumer looking to buy a home. To qualify for a mortgage, the applicant generally had to provide a 20 - 25% down payment, and the monthly payment could not exceed 30% of gross income. Lenders used loan officers rather than mortgage brokers for most transactions.
In an effort to prevent redlining and to meet the needs of low- to moderate-income groups, various federal regulations were enacted, beginning with the Community Reinvestment Act of 1977, which measured each financial institution's performance within defined areas. Non-compliance at that time could result in severe consequences.

Savings and Loan Crisis of the 1980s and 90s

Due to spiraling inflation in the late 1970's, the Federal Reserve Bank doubled the interest rate by restricting the growth of the money supply, which in turn caused interest rates to skyrocket. Between June 1979 and March 1980, short-term interest rates rose by more than six percentage points. Low income on the inventory of existing mortgages vs. high interest on short term savings accounts resulted in extraordinary losses by the thrift institutions. In order to curtail the crisis, new federal rules allowed for expanded investment options and eliminated interest ceilings for the thrifts until such time that interest rates returned to normal.

As a result of those risky investments, high interest rates and the transition from traditional mortgages to more risky investments, over 118 savings and loan associations failed in the next three years; and it is estimated that this move ultimately cost taxpayers over $150 billion dollars.[1]

The Creation of FIRREA and Title XI

In the wake of the Savings and Loan crisis, Congress responded by enacting more legislation. It began in 1987 with Congressman Doug Barnard Jr. of Georgia introducing H.R. 3675, the Real Estate Appraisal Reform Act. This bill gave a major role to The Appraisal Foundation and established the Federal Interagency Appraisal Counsel to set real estate appraisal standards and qualifications for transactions in which the federal government has substantial financial or public policy interests. Because Congressman Barnard feared the bill would fail, he decided to use the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) as a vehicle for appraisal reform; and he inserted his bill as a separate amendment known as Title XI in FIRREA.

FIRREA dramatically changed the S&L industry and its federal regulation, including title insurance. Title XI required that appraisals utilized in connection with federally related transactions be performed in writing, in accordance with uniform standards, and by competent individuals whose professional conduct was subject to effective supervision. In addition, it established the Appraisal Subcommittee (ASC)[2] to monitor the activities of the state regulatory agencies and The Appraisal Foundation, which promulgates the generally accepted appraisal standards and qualification standards for state licensed and certified appraisers. FIRREA also upgraded and consolidated the regulations of various federal agencies.

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[1] House Committee on Government Operations, *Impact of Appraisal Problems on Real Estate Lending, Mortgage Insurance, and Investment in Secondary Market*, 99th Congress, 2nd session, 1986, H. Rep. 99-891, 4-6.

[2] Responsibilities of the Appraisal Subcommittee (ASC)
The Appraisal Subcommittee (ASC) maintains a National Registry of Appraisers and transmits a report to Congress annually detailing the activities of the ASC. It also provides federal oversight of State appraiser regulatory programs and provides a monitoring framework for The Appraisal Foundation and the Federal Financial Institutions Regulatory Agencies in their roles to protect federal financial and public policy interests in real estate appraisals utilized in federally related transactions.
111th Congress, *Dodd-Frank Wall Street Reform and Consumer Protection Act*.
https://www.sec.gov/about/laws/wallstreetreform-cpa.pdf

We do believe that generally Title XI of FIRREA and the establishment of the Appraisal Subcommittee provided effective regulatory oversight and that The Appraisal Foundation has been an effective, independent organization allowing for standardized rules within the profession.

The Subprime Mortgage/Financial Crisis of 2007-2008

The Housing and Community Development Act of 1992 amended the charter of both Fannie Mae and Freddie Mac to facilitate the financing of affordable housing for low- and moderate-income families. Again in 1999, more pressure was exerted on the financial institutions through the Community Reinvestment Act to expand mortgages and to ease credit requirements. This action adversely resulted in the financial institutions lowering their underwriting standards, offering interest-only loans and floating/adjustable rates (in some cases with little or no documentation to support the consumer's ability to repay the loan.)

These high-risk loans came with higher interest rates; and the financial institutions began a radical move to *mortgage-backed securities* with earnings dependent on volume. The share of subprime mortgages to total originations increased from 9 percent in 1996 to 20 percent in 2006, according to Forbes. Subprime mortgages totaled $600 billion that year; and lenders held very few, if any, of these loans in their own portfolios. They were indeed reaping the benefits of these new high-risk investments without being held responsible for any of the risk.[3]

The secondary mortgage market, which includes collateralized debt obligations (CDOs), soared, and CDOs exploded from $75 billion in 2003 to $450 billion in 2006. These securities were backed by AAA ratings. It appears that rating agencies did not do their jobs and that investors did not do their due diligence.

Regrettably, the relaxed standards for mortgage loans and the movement to mortgage-backed securities led to the Subprime Mortgage/Financial Crisis of 2007-2008 for subprime, Alt-A, CDOs, mortgage, credit, hedge fund, and foreign lending markets. In October 2007, the U.S. Secretary of the Treasury Henry Paulson called the bursting housing bubble that led to the crisis "the most significant current risk"[4] to the US economy. It was a catastrophe caused by many players, including some appraisers. Overall, appraisers contributed

[3] Ginnie Mae was a main participant in the mortgage crisis of 2008. Ginnie Mae's most important program was and is the mortgage-backed security program in which Ginnie Mae guarantees pools of mortgages accumulated by mortgage originators of "low- and moderate-income households across America by channeling global capital into the nation's housing markets."
Ginnie Mae Home, *Who we are. What we do. Why it makes a difference*, http://ginniemae.gov/pages/default.aspx
[4] Housingwire, *Paulson: Housing a 'Significant Risk' to Economy*, October 16, 2007.
http://www.housingwire.com/articles/paulson-housing-significant-risk-economy

relatively little but were assigned a significant amount of the blame.
As a result of the financial crisis, the Attorney General of New York State, Andrew Cuomo, began an investigation into the practices of Fannie Mae and Freddie Mac. Subsequently, Fannie Mae and Freddie Mac signed a settlement with Cuomo, agreeing to abide by new rules which would be embodied in the Home Valuation Code of Conduct (HVCC) that went into effect in May 2009. As part of the agreement, Cuomo's investigation into Fannie Mae and Freddie Mac's practices was terminated. With the co-signing of the agreement by the Office of Federal Housing Enterprise Oversight, HVCC was given federal rule status.

HVCC was designed to protect appraiser independence and prevent pressure on appraisers to produce a desired property value. It was also intended to protect consumers. Compliance with the rules was required for all loans backed by Fannie Mae or Freddie Mac. Most of the big appraisal organizations initially backed the policy; but by the end of the comment period (45 days) had reversed their stances and submitted commentary much more critical of HVCC than their original comments. The rules stayed in effect and were eventually incorporated, in part, into the next big legislation, the Dodd-Frank Wall Street Reform and Consumer Protection Act, signed into law in July 2010.

While we believe that the reforms enacted by Title XI of FIRREA were good reforms and provide oversight and controls similar to those of many other licensed professions, the rules implemented as a part of the Home Valuation Code of Conduct (HVCC) and incorporated into Title XI as amended by the Dodd-Frank Reform Act have in many cases resulted in unintended consequences. We will discuss these unintended consequences in Part 2 of this document.

Dodd-Frank/Wall Street Reform and Consumer Protection Act

Dodd-Frank was signed into federal law on July 21, 2010, in response to the Subprime Mortgage/Financial Crisis of 2007-2008 and the subsequent Great Recession that followed. The legislation brought the most significant changes to financial regulation in the United States since reforms following the Great Depression. The reforms affected all federal financial regulatory agencies and almost every part of the nation's financial services industry, including appraisers.

How did Dodd-Frank affect the financial services industry, including appraisers?

1. Expanded the functions of the Appraisal Subcommittee (ASC) to include monitoring of State requirements for registration/supervision of operations/activities of appraisal management companies
2. Required the ASC to report to Congress annually regarding activities of the ASC, including results of all audits of State appraiser certifying and licensing agencies
3. Mandated national registry of appraisal management companies registered with and subject to supervision of State appraiser certifying and licensing agencies
4. Set up grants available through ASC for State appraiser certifying and licensing

agencies to support the efforts of such agencies to comply with Dodd-Frank
5. Established that appraisals be subject to appropriate review for compliance with the Uniform Standards of Professional Appraisal Practice
6. Authorized that thresholds established by financial institutions regulatory agencies and The Resolution Trust Corporation concur with Bureau of Consumer Financial Protection to provide reasonable protection for consumers who purchase 1-4 unit family residences
7. Set new rules based on size and complexity of appraisal requiring the services of State certified appraisers
8. Set minimum qualifications for Trainee Appraiser and Supervisory Appraiser through AQB
9. Gave ASC the authority to remove State licensed or certified appraiser from the national registry for a period not to exceed 90 days, pending State agency action on licensing, certification, registration and disciplinary proceedings
10. Established limitations on appraising through reciprocity based on State policy
11. Prohibited discrimination against consideration of appraiser for an assignment based solely on membership in a nationally recognized professional appraisal organization
12. Mandated ASC monitoring of State appraiser certifying and licensing agency for the purpose of maintaining appraiser independence
13. Encouraged States to accept courses approved by AQB Course Approval Program
14. Set up Complaint National Hotline to receive complaints of non-compliance with appraisal independence standards and Uniform Standards of Professional Appraisal Practice (to address improper influence or attempted improper influence of appraisers or the appraisal process)
15. Set requirements for Appraisal Management Companies including registration with State appraiser certifying and licensing agencies
16. Set standards for Automated Valuation Models (AVMs) and limitations on use of Broker Price Opinions (BPOs)
17. Required customary and reasonable compensation for appraisers
18. Mandated additional provisions for high-risk mortgages, including interior inspections of subject properties by licensed or certified appraisers

Part 3 – Challenges, Problems and Proposed Remedies

According to data available from the United States Census Bureau and published in an April 2013 article by the Appraisal Institute, the number of appraisers nationwide peaked in 2007 at 118,657. The ASC lists the current number of appraisers at 100,129 as of April 2015. Although these statistics represent total credentials rather than the actual number of appraisers (i.e. an appraiser may be counted multiple times if he/she is credentialed in multiple states), the trend is clear. There has been a decline in appraiser credentials of more than 15% over the 6-plus year period.

The decline is due in part to age attrition and fewer new entrants into the field. Another reason cited for the drop in appraiser credentials is increased use of alternative valuation products and/or broker price opinions (BPOs) by lenders. These factors, coupled with overall challenging business conditions and convoluted new government regulations, have led to limited growth opportunities in the real estate appraisal profession.

At the same time the appraisal profession is becoming more challenging for current appraisers, educational requirements are becoming stricter. According to a January 2012 report to Congress from the Government Accountability Office (GAO), "Title XI of FIRREA (as amended by Dodd-Frank) created a complex regulatory structure that relies upon the actions of many state, federal and private entities to help ensure the quality of appraisals and the qualifications of appraisers used in federally related transactions."[5]

One of the primary barriers facing appraisers entering the appraisal profession as of January 2015 is increased educational requirements, including

- For Licensed Residential appraisers, increasing formal education requirements from no degree requirement to "an Associate's degree or higher (in any field) from an accredited college, junior college, community college , or university"[6]

- For Certified Residential appraisers, increasing formal education requirements from "Associate's degree" to "Bachelor's degree or higher (in any field) from an accredited college or university"[7]

Listed below are the requirements already in effect for licensed and certified appraisers:

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[5] Government Accountability Office, *Highlights of GAO-12-147, a report to congressional committees*, January 2012, page 8.
[6] The Appraisal Foundation, *New! Summary of Changes to the Real Property Appraiser Qualification Criteria (effective January 1, 2015).*
https://netforum.avectra.com/eweb/DynamicPage.aspx?Site=taf&WebCode=RPCriteria
[7] Government Accountability Office.
https://netforum.avectra.com/eweb/DynamicPage.aspx?Site=taf&WebCode=RPCriteria

For a Licensed Residential appraiser:

- 2,000 hours of experience obtained in no fewer than 12 months
- 150 creditable class hours (7 courses) in appraisal-specific subjects
- passing a standardized Appraisal Qualifications Board (AQB) exam and
- 28 credits of appraiser-specific continuing education every two years.

For a Certified Residential appraiser:

- 2500 hours of experience obtained in no fewer than 24 months
- 200 creditable class hours (10 courses) in appraisal-specific subjects
- passing a standardized Appraisal Qualifications Board (AQB) exam and
- 28 credits of appraiser-specific continuing education every two years

While there may be some rationale for higher educational requirements, the additional requirements listed above have made the process of becoming an appraiser more burdensome. (See footnote.[8])

Throughout the rest of this paper we will explore various factors that have influenced the decline in credentials and give recommendations of how to improve the attractiveness of the profession to new entrants while protecting consumers.

Problem 1 – Trainees Face Training Hurdles

In today's market, for federally related transactions, lenders and AMCs do not typically accept work from anyone other than licensed or certified appraisers. This practice leaves appraisal trainees with no way to earn the work experience required by law. This structure discourages established appraisers from hiring Appraiser Trainees. The profession must take on the responsibility for training new entrants; otherwise, there will be too few appraisers remaining to assume responsibility from those retiring.

A survey done in June 2013 by the Appraisal Institute showed that trainee hiring will remain relatively weak for the next one to two years, based mainly on lenders/AMCs resistance to

[8] The basis for this change (higher educational requirements) is that individuals with higher educational levels have typically tested better on the AQB-approved examination. Test results also indicate that individuals with Bachelor's degrees or higher perform better on the exam than those with Associate degrees or without degrees. (The previous statements have been supported by demographic information on candidates sitting for exams in January 2010).
Appraiser Qualifications Board, *Proposed Revisions to the Future Real Estate Appraiser Qualification Criteria*, October 28, 2010.

having trainees do any work. Of those surveyed only 9 percent of residential appraisers plan to hire more trainees during this period.[9]

Recommendation:
The Appraisal Qualifications Board (AQB) currently has in place qualification criteria for Appraiser Trainees that gives clear guidelines for trainees and the supervisory appraisers who oversee them. Quality training programs need to be designed and implemented to support and link the educational and experience requirements for appraising.

In one model, appraisal students could spend the first two years of a four-year degree program learning general and appraisal-specific concepts, followed by two years of a combined education/work experience program, thus allowing students to graduate with the qualifications necessary for becoming a certified appraiser.

We feel that it is important to also encourage lenders and AMCs to adopt policies regarding trainees and supervising appraisers and not insist that trainees be accompanied on inspections beyond the point where they are considered competent by their supervising appraisers.

Problem 2 – Lack of Mandatory State Licensing in All States

A reported issued in 2012 by the Government Accountability Office (GAO) to Congress stated that "Under authority granted by Title XI, the federal regulators also have adopted regulations that exempt federally related transactions of $250,000 or less from appraisal requirements"[10] (meaning that the services of a licensed or certified appraiser are not required). Fannie and Freddie were also deemed exempt.

The fact that licensed or certified appraisers are not required for the majority of mortgages leaves consumers at risk. The GAO in January 2012 found that "more than 70 percent of residential mortgages made from 2006 through 2009 were $250,000 or less."[11]

As previously discussed, a residential appraisal license/certification takes years of training, education and experience to acquire. Lenders, in order to save money and meet federal requirements, are using alternatives to appraisals to obtain values on homes. Many utilize Broker Price Opinions (BPOs) in part for refinances.

It should be noted that real estate salespersons and brokers in New York State, as an example, have no formal education requirements (whereas certified appraisers will require a bachelor's

[9] Appraisal Institute, *2013 Appraisal Outlook*, June 28, 2013
[10] Government Accountability Office, *Highlights of GAO-12-147, a report to congressional committees*, January 2012, page 23.
[11] Government Accountability Office, *Highlights of GAO-12-147, a report to congressional committees*, January 2012.

degree in 2015), no work experience requirements for salespersons and only two years' work experience as a salesperson to qualify as a broker (certified residential appraisers require 2,500 hours experience in no less than 24 months). Salespersons and brokers are not required to complete any appraisal related coursework or appraisal continuing education (certified residential appraisers require 200 hours of appraisal related coursework and 28 hours of appraisal continuing education every two years).

Lack of consistency in state licensing requirements leaves consumers vulnerable to comparability and reliability issues. Presently, only 37 licensing jurisdictions require mandatory licensing, and the rest are either voluntary or mandatory for federally related transactions only. Another issue associated with transparency is the lack of disclosure about the components covered by the appraisal fees, such as lender fees, fees paid for AMC services, and direct appraisal fees.

Recommendation:
We propose mandatory licensing rules be put in place and enforced in all states, requiring the use of licensed or certified appraisers for any services for which an opinion of value for real property is developed. Mandatory licensing in all states would improve the comparability and reliability of appraiser valuations nationwide, supporting consumer's need for better information during the home buying process. It is also our opinion that each component of the appraisal fee should be listed separately when disclosed to the client, so that consumers know fully where their money goes as part of the overall mortgage transaction.

Problem 3 – The Federal De Minimis Limit is Set Too High

The de minimis appraisal threshold, the dollar level set by the federal financial regulators to exempt real estate loans made by federally insured financial institutions from statutory appraisal requirements, was increased in 1994 from $100,000 to $250,000 as a way to reduce regulatory burden and encourage economic growth. Though many groups have lobbied to reduce the de minimis since that time, none have been successful except in one type of mortgage loan, the Higher-Priced Mortgage Loans (HPML)[12].

Mortgage loans are HPMLs if they are secured by a consumer's principal dwelling and have annual percentage rates (APRs) that exceed the Average Prime Offer Rate (APOR) by 1.5 percentage points or more (see footnote for reference to additional criteria[13]). In other words, HPMLs are high-interest loans.

[12] TILA Regulation Z defines HPML's as: "a consumer credit transaction secured by the consumer's principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 or more percentage points for loans secured by a first lien on a dwelling, or by 3.5 or more percentage points for loans secured by a subordinate lien on a dwelling."
Consumer Financial Protection Bureau, *TILA Higher-Priced Mortgage Loans (HPML) Appraisal Rule*, January 13, 2014, http://files.consumerfinance.gov/f/201401_cfpb_tila-hpml_appraisal-rule-guide.pdf
[13] Consumer Financial Protection Bureau, http://files.consumerfinance.gov/f/201401_cfpb_tila-hpml_appraisal-

It is important to note that in December 2012, the Federal Register discussed HPMLs and established a $25,000 de minimis for these loan types. In January 2013, after the Final Rule was issued, a consumer advocacy group expressed the view that "LMI (lower- to middle-income) consumers obtaining or refinancing loans secured by lower-value homes may have a particular need for the protections of the HPML."[14] When the final rule was issued, the de minimis for HPMLs was set at $25,000, or 1/10 that established for all other federally related transactions. The de minimis for all other mortgage loans has remained at $250,000.

Data analyzed for this paper, taken from the S&P Case-Shiller 20-City Home Price Index for the period 2009-2015, indicate that the average price for homes in surveyed markets ranged between $140,000 and $175,000.[15] The data show that, at a minimum, most residential real estate transactions are below the de minimis, thereby nullifying the federal requirement for an appraisal. Thus, many consumers are effectively being denied the right to professional appraisals in a significant amount of mortgage transactions.

Recommendation:
We propose that the existing de minimis threshold of $250,000 for all federally related mortgage transactions be lowered to the $25,000 HPML Appraisal Rule passed by the combined efforts of the Department of the Treasury, Board of Governors of the Federal Reserve System and the Bureau of Consumer Protection. Reducing the de minimis threshold would increase the number of transactions requiring professional appraisals, giving more consumers access to more reliable valuations.

Problem 4 – Lack of Regulation Concerning Customary and Reasonable Fees

The level of fees paid to appraisers is clearly one of the most important issues facing the profession. Declining fees currently being paid by AMCs to appraisers have discouraged new entrants from coming into the profession.

Dodd-Frank requires that lenders and their agents compensate fee appraisers at a rate that is *customary and reasonable* for appraisal services – customary as it pertains to the market area and reasonable as it pertains to the complexity of the specific appraisal. The law allows for two alternatives approaches when determining rates: 1) that the rate be "reasonably related to recent rates paid for comparable appraisal services performed in the geographic market of the property being appraised" or 2) that the rate be established "by relying on information about rates that Is based on objective third-party information, including fee schedules, studies, and surveys prepared by independent third parties such as government agencies, academic

rule-guide.pdf
[14] Federal Register, Vol. 78, No. 248, December 26, 2013. 78529.
[15] Federal Reserve Bank of St. Louis, *S&P Case-Schiller 20 City Home Price Index*, 2014. https://research.stlouisfed.org/fred2/series/SPCS20RSA, January 2000.

institutions, and private research firms."[16]

In our research we found little actual data indicating that AMCs are paying *customary and reasonable* fees. Instead, many appraisers have stated that AMCs shop the marketplace for rock-bottom prices. The process is as follows: an AMC sends an email blast to all appraisers within a given area, detailing the property and offering a certain fee for the completion of the assignment within a prescribed time frame. The email may or may not even discuss assignment elements that an appraiser must consider in order to make an appropriate scope of work decision for the assignment. Time frames offered are many times less than what the appraisal actually entails. Appraisers receiving the email are left with one choice: accept the assignment as-is, at the fee being offered, in the time-frame being given. If an appraiser tries to counter with a higher fee, invariably the AMC has already hired someone else based on the original fee and timeframe requested.

Another concern is whether or not AMCs are addressing the "reasonable" aspect of *customary and reasonable*, the things that make an appraisal more complex and time consuming than the average, things like location, size, driving distance, availability of comparable data, and access to sales contracts and other information supplied by third parties.

To help address these problems, Dodd-Frank requires that State appraiser certifying and licensing agencies register and oversee AMCs. At least one state, Louisiana, has gone a step further in dealing with the *customary and reasonable* debate. In May, 2012, Louisiana passed its *Louisiana Appraisal Management Company Licensing and Regulation Act*. The law requires that AMCs "compensate appraisers at a rate that is *customary and reasonable* for appraisals in the market area of the property being appraised, consistent with the presumptions of compliance under federal law."[17]

To determine what constitutes *customary and reasonable* fees, Louisiana authorized a statewide survey done by the Southeastern Louisiana University Business Research Center. The survey focused on fees being paid by lenders, not AMCs, to determine *customary and reasonable* fees for specific assignments in specific areas. The survey also included appraiser input for comparison. The final results of the survey set the standard for customary rates in various regions of Louisiana. Although AMCs operating in Louisiana are not bound to the rates prescribed, they are required to provide extensive documentation on how the rate used was developed if audited.

The question relating to the proper methodology to determine *customary and reasonable* fees has been an issue since they were mandated by Dodd-Frank. In a Division of Consumer and Community Affairs report dated October 28, 2010, appraiser representatives and one state legislator argued that creditors and AMCs rely on published fee studies such as Veterans

[16] http://www.sec.gov/about/laws/wallstreetreform-cpa.pdf

[17] Louisiana Real Estate Appraisers Board, *AMC Licensing and Regulation Act*, Acts 2009, No. 502, §1, eff. Jan. 1, 2010, http://www.reab.state.la.us/AMC_license_law.html

Administration fee schedules to determine how much to pay appraisers. Creditors and AMCs argued that VA fees were too high for "average appraisals." We disagree with the creditors and AMCs.[18]

It has been suggested that the Veteran Administration's (VA) fee schedule fairly reflects, at a minimum, fees associated with the work involved in appraisal development and reporting, as well as time frame (7 to 10 days in most markets), and other requirements to develop and report credible and USPAP-compliant appraisals.

Recommendation:
We suggest that all states follow the Louisiana AMC law and begin regulating AMCs as Dodd-Frank mandates. Furthermore, states should follow the Louisiana model and conduct their own independent studies to determine what *customary and reasonable* fees should be for their geographic areas. Where studies have not yet been developed, we suggest the use of VA rates as an alternative.

Problem 5 – Lack of Communication between Clients and Appraisers

The lack of understanding regarding communication between the client and the appraiser became even more prevalent after the enactment of Dodd-Frank. Lenders quickly promoted AMCs as middlemen, and AMCs quickly and happily accepted this new and growing business. Actually, Dodd-Frank never restricted communication between the client and the appraiser; instead, its intent was to protect the independence of the appraiser and the appraisal process.

In addition, Dodd-Frank, TILA, GSE Servicing guidelines and USPAP all address appraiser/agent communications. None prohibit appraisers from speaking with real estate agents during the appraisal process. Agents may talk with appraisers and provide additional property information, including a copy of the sales contract for purchase transactions. Of course an agent must not intimidate or bribe an appraiser, and an appraiser must not disclose confidential information at any time. (See footnote for Dodd-Frank language on this topic.[19])

Once an appraisal assignment is completed and sent to the client, USPAP prohibits an appraiser from discussing the results of the report with anyone other than the client or parties designated

[18] Federal Reserve Board Staff, *Docket No. R-1 3 9 4 - Valuation Independence Interim Final Rule (12 CFR 226.42)*, October 28, 2010.

[19] "The requirements of subsection (b) shall not be construed as prohibiting a mortgage lender, mortgage broker, mortgage banker, real estate broker, appraisal management company, employee of an appraisal management company, consumer, or any other person with an interest in a real estate transaction from asking an appraiser to undertake 1 or more of the following:

- Consider additional, appropriate property information, including the consideration of additional comparable properties to make or support and appraisal.
- Provide further detail, substantiation, or explanation for the appraiser's value conclusion.
- Correct errors in the appraisal report."

111th Congress, https://www.sec.gov/about/laws/wallstreetreform-cpa.pdf by the client. At this point no one except the client can ask for corrections or request consideration of additional data. (See footnote for USPAP Ethics Rule language on this topic.[20])

Recommendation:

We believe that it is important that underwriters who are responsible for verifying credibility and USPAP compliance of appraisal reports be allowed and encouraged to communicate directly with the appraiser. This would eliminate much of the confusion and promote efficient time usage in the appraisal process by reducing the amount of information and questions passed through AMCs to either the underwriter or the appraiser. A more efficient process would benefit the consumer.

Problem 6 – New Regulations Dilute the Appraisal's Importance in Loan Underwriting

New regulations enacted by the Consumer Financial Protection Bureau, entitled *Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z)* state that "The act (Appraisals for Higher-Priced Mortgage Loans {HPML Act}) contains special appraisal requirements with respect to higher-risk mortgages"[21]. The HPML regulations contain language regarding a $25,000 *de minimis* and include very specific appraisal standards for higher-priced mortgage loans. It is troubling that the Qualified Mortgage regulations further imply that the following are exempt from these appraisal requirements:

- Qualified Mortgages (Unclear what, if anything, is required);
- Higher-priced mortgages with a debt-to-income ratio of 43 or less;
- Loans with a higher debt to income ratio that are purchasable by the GSAs or insurable by FHA (this is presumably a temporary provision).

The above three exclusions effectively remove the preponderance of loans from any defined appraisal requirements.

With this in mind, the Qualified Mortgage regulations conclude that "The impact of this reduction in the scope of appraisal requirements is relatively muted for first lien mortgages because of the small number of high-risk mortgages to begin with and the fact that most lenders already do a full interior appraisal and share the results with the consumer".[22]

[20] "An appraiser must not disclose 1) confidential information or 2) assignment [appraisal] results to anyone other than the client, persons specifically authorized by the client, state appraiser regulatory agencies, third parties as may be authorized by due process of law, or a duly authorized professional peer review committee except when such disclosure to a committee would violate applicable law or regulation."
111th Congress, https://www.sec.gov/about/laws/wallstreetreform-cpa.pdf

[21] Bureau of Consumer Financial Protection, *Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z)*, January 10, 2013..

[22] Bureau of Consumer Financial Protection, *Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act (Regulation Z)*, January 10, 2013.

Recommendation:
It is our opinion that in underwriting a loan, the parties responsible for underwriting the loan should critically analyze the value of the property, the condition of the property and the borrower's ability to repay the loan. Historically, when lenders wrote mortgages they considered all three aspects very carefully since they were responsible for the property if a loan defaulted. Ideally, lenders would be held responsible for failed loans within a reasonable time period (e.g. five years). This would ensure a critical review of all three criteria. However, this option was considered and not implemented by Dodd-Frank. In the absence of this alternative, it is imperative to ensure that lenders are responsible for ensuring that all loans in excess of the *de minimis* be held to the same standards as the higher-priced mortgages with regard to property valuation/condition. It is not acceptable to simply state that "most lenders already do a full interior appraisal ...." If this standard is not applied to each and every mortgage written, consumers and ultimately taxpayers are placed in jeopardy. Furthermore, lenders and not the AMCs must be held accountable for underwriting the risks associated with these loans, including the accuracy of appraisals. This approach will contribute to ensuring that low cost and fast turnaround are not the basis for choosing qualified appraisers.

Problem 7 – How the Appraiser is Viewed by the Consumer and the Public Generally

Though consumers have a vague understanding of the appraisal process, they do not understand that one of the appraiser's main roles in the loan process is to protect the consumer. Appraisers have been unjustifiably blamed for "killing the deal" if the value comes in too low to satisfy the loan requirements.

Recommendation:
There are numerous pamphlets and flyers that explain the appraisal process to consumers; however, they are not being distributed widely. While The Appraisal Foundation is working closely with a public relations firm to promote the profession, federal and state governments must also participate in this educational process; financial institutions should be required to disseminate this information when accepting loan applications; and professional appraisal organizations could also support consumer education with wider distribution of educational and informational materials.

Problem 8 – Poor Implementation of AMC Regulation and Oversight

We believe that, while Dodd-Frank put heavy regulation on appraisers, there is insufficient regulation of the middlemen, the appraisal management company (AMC)

The FDIC, in its Interagency Evaluation and Appraisal Guidelines, talks about third party arrangements in which a lender engages a third party (AMC) to perform real property valuation-related services, such as selecting an appraiser to perform an appraisal. In those cases it is the responsibility of the lender to understand and manage the risks associated with the arrangement. The Guidelines caution that an institution should have the resources and expertise necessary for performing ongoing oversight of third party arrangements. They go on to say that "An institution also is responsible for ensuring that a third party selects an appraiser or a person to perform an evaluation who is competent and independent, has the requisite experience and training for the assignment, and thorough knowledge of the subject property's market."[23]

But the question is, "Are lenders doing their due diligence in overseeing AMCs; and if not, are the States?" Some States have undertaken the task of regulating AMCs, but not enough has been done in this area. While this will be addressed through the requirements placed on states to regulate AMCs under Dodd-Frank, the laws of each state will go a long way to determining how effective AMC regulation will ultimately prove.

We also recommend that lenders be held to their new responsibilities as created by Dodd-Frank. If lenders remain in charge of the lending and appraisal process, they will be less likely to rely on AVMs and BPOs and will instead look for quality appraisals done by licensed or certified appraisers.

[23] Federal Deposit Insurance Corporation, *Interagency Appraisal and Evaluation Guidelines*, https://www.fdic.gov/regulations/laws/rules/5000-4800.html

Problem 9 – Unreasonable Timeframe for Lenders to Estimate Appraisal Fees

There has been a change in the interpretation of the three-day requirement for estimates by lenders as a part of a 2014 TILA-RESPA Integrated Disclosure Rule that has made it very difficult for the lenders to select the most qualified appraiser at a reasonable and customary fee.

The problem is that the 1974 law entitled RESPA stated:

> "(c) Estimate of charges
> Each lender shall include with the booklet a good faith estimate of the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement as prescribed by the Secretary.
>
> (d) Distribution by lenders to loan applicants at time of receipt or preparation of applications
>
> Each lender referred to in subsection (a) of this section shall provide the booklet described in such subsection to each person from whom it receives or for whom it prepares a written application to borrow money to finance the purchase of residential real estate. Such booklet shall be provided by delivering it or placing it in the mail not later than 3 business days after the lender receives the application, but no booklet need be provided if the lender denies the application for credit before the end of the 3-day period."[24]

The 2014 TILA-RESPA Integrated Disclosure Rule replaced the 1974 RESPA language shown above, and while still stating that the "creditor is required to provide the consumer with good-faith estimates (underline added for emphasis) of credit costs and transaction terms in Section 5.1 of the Small Entity Compliance Guide, it states that "Creditors generally may not issue revisions to Loan Estimates because they later discover technical errors, miscalculations, or underestimations of charges." [25] Furthermore, In Section 7.1 of the document it is made clear there is little tolerance for revision of the "estimate" where the rules state that:

> Generally, if the charge paid by or imposed on the consumer exceeds the amount originally disclosed on the Loan Estimate it is not in good faith, regardless of whether the creditor later discovers a technical error, miscalculation, or underestimation of a charge.

It is not difficult to estimate the cost of such services as routine credit reports, flood certifications, tax services, etc. since they are fairly well standardized; however, this is not true of an appraisal. In most cases, location, complexity of the valuation and scope of work cannot

[24] HUD website, http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/rmra/res/resp2604
[25] ConsumerFinance website, http://files.consumerfinance.gov/f/201403_cfpb_tila-respa-integrated-disclosure-rule_compliance-guide.pdf

be immediately determined. However, in order to comply with the 2014 TILA-RESPA rules, lenders are forced to quickly obtain and guarantee a fee. An easy way to do this is to utilize the services of an appraisal management company that sends out email requests and generally accepts the lowest bidder providing the fastest turnaround. Time simply does not allow either the lender or the appraisal management company to analyze and determine a reasonable and customary fee done by the most competent and experienced appraiser in the time allowed.

Recommendation:
To solve this problem, the lenders should be given more flexibility in estimating the appraisal fee within the three day period, and not be held to such strict requirements as it pertains to upward adjustments in the cost of the appraisal. Where a state has performed an appraisal fee study, lenders may be better situated to provide more accurate estimates; as such, it is imperative that states engage in fee studies not only for the benefit of appraisers, but for consumer confidence in the estimated fee.

Part 4 – Conclusion

Unfortunately, a small number of real estate appraisers played a role in the Subprime Mortgage/Financial Crisis of 2007-2008; however, their part was not commensurate with the heavy toll the appraisal profession took legislatively. Some of the legislation, while well intentioned, had negative consequences that are affecting the livelihoods of appraisers, especially residential appraisers, and threatening the future of the profession in general. More importantly, consumers are paying the price as well.

Many appraisers are leaving the profession due to heightened regulations, undue interference by AMCs, low pay, and other factors not necessarily discussed in this paper. New entrants are not coming in due to a variety of reasons, including new and heightened educational standards that went into effect on January 1, 2015.

Lenders are relying more heavily on third parties (AMCs) in overseeing the appraisal process. Dodd-Frank puts lenders in charge of managing the risks associated with AMCs, including the lender's obligation to insure that AMCs hire appraisers based on competence, independence, and thorough knowledge of the subject property's market. If lenders understand and accept their obligations in this area, they may be willing to rely less on BPOs or AVMs performed by non-appraisers and ask for quality appraisals by licensed and certified appraisers instead.

Lenders should be held responsible for loans that they underwrite and process even where the loan is sold to third parties such as Fannie Mae and Freddie Mac. If a loan fails within the first five years, the lender should be held responsible for the full amount of the balance of the loan. If this is required, lenders will insist on reasonable underwriting standards and quality appraisals.

Regulatory Issues Facing the Real Estate Appraisal Profession

AMCs have to be regulated consistently state to state, not haphazardly as is now the case. Appraisers should not be the only party who has to abide by the rules of USPAP. All parties participating in federally related mortgage transactions should adhere to the same ethical standards as appraisers.

Some AMCs have created communication wedges between lenders and appraisers due to lack of understanding of the rules. This lack of communication has hurt the appraisal process in general. The resistance of lenders and AMCs to allow appraiser trainees to perform work is another barrier. Low fees and illogical turnaround time requirements for work performed by residential appraisers have further compromised the appraisal process and quality of the product.

Mandatory state licensing would go a long way to alleviate some of the problems created by Dodd-Frank and Title XI. It would require the use of licensed and certified appraisers for all federally related mortgage transactions involving appraisals and appraisal reviews, in lieu of brokers/salespersons and others who are not as knowledgeable or experienced. Lowering the de minimis to $25,000 would also be beneficial.

In the end, the consumer pays the ultimate price. This fact cannot be overemphasized. The entire reason for Dodd-Frank was to protect the consumer, as well as the independence of the appraiser. Due to unintended consequences, the law has done neither. It is the responsibility of all parties involved in the mortgage lending process - legislators, regulators, lenders, AMCs, nonprofit appraisal organizations, and appraisers – to understand and correct the current deficiencies in the law.

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NATIONAL ASSOCIATION OF INDEPENDENT FEE APPRAISERS
NAIFA

A White Paper on the Federal Banking Agencies' Arbitrary and Capricious Efforts to Exempt the Vast Majority of Federal Real Estate Related Financial Transactions from Title XI of FIRREA's Appraisal Reforms

June 13, 2016

EXECUTIVE SUMMARY

The banking agencies, led by the FDIC, have recently taken the position that the vast majority of real estate related financial transactions in which the government has a safety and soundness or a consumer protection responsibility are exempt from Title XI..[1] They have made clear that under their restrictive interpretation of Title XI's "federally related transaction" phrase, the appraisal law does not apply to or protect the hundreds of billions of dollars in mortgage loans guaranteed by the FHA, the VA or USDA's rural housing program; the mortgages purchased and sold by Fannie Mae or Freddie Mac; and, any originated mortgage which even qualifies for sale to a GSE. This shocking interpretation of Title XI – which places the overwhelming majority of all residential mortgages beyond the law's protections – surfaced and became clear only recently when it was announced by a representative of the FDIC at an April 2016 meeting of state appraiser licensing agencies. As word of the FDIC's Title XI interpretation spread, it stunned federal agencies which have relied for many years on the law's provisions as well as its private sector stakeholders.

The FDIC (and, it seems, the other federal banking agencies) argue that they exempted these transactions in their 1994 Appraisal and Evaluation Guidelines by declaring that they are not "federally related transactions" within the meaning of the law. This position is indefensible and flat-out wrong. As explained in some detail below, the banking agencies' current interpretation of Title XI is directly contradicted by the following facts –

(1) **All Title XI stakeholders disagree:** All Title XI stakeholders at the state and federal levels of government and in the private sector have had a common understanding for 25 years that the law was intended to be broad-based and that it applied to all real estate related financial transactions. This

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[1] Under Title XI, the term "real estate-related financial transaction" means "any transaction involving—
(A) the sale, lease, purchase, investment in or exchange of real property, including interests in property, or the financing thereof;
(B) the refinancing of real property or interests in real property; and
(C) the use of real property or interests in property as security for a loan or investment, including mortgage-backed securities."

common understanding existed prior and subsequent to issuance of the 1994 Appraisal Guidelines and continues to this day; (See page 7 for more detail)

(2) **The federal banking agencies have never objected, until now, to the broad interpretation of Title XI's reach that the state appraiser licensing agencies, the government's housing and mortgage insurance agencies and the federal Appraisal Subcommittee have observed for decades:** It is important to recognize that while the banking agencies now contend they exempted the vast majority of real estate related financial transactions from Title XI in 1994, they have known for dozens of years that the state licensing agencies and the federal Appraisal Subcommittee were exercising their Title XI responsibilities as applying broadly across government agencies and that the government's housing and mortgage guaranty/insurance agencies had depended on and had benefitted from Title XI's protections – yet the federal bank regulators never objected. They never once told these state and federal entities that their interpretation of the appraisal law was in conflict with their regulatory Guidelines and was, therefore, invalid. The banking agencies' "say nothing, do nothing" stance until now demonstrates that their current interpretation of "federally related transaction" is actually a reinterpretation of the law that is arbitrary and capricious;

(3) The legislative history of Title XI Is conclusive that Congress intended the law to apply broadly across all government housing and mortgage programs: The conditions which gave rise to Title XI as well as its legislative history clearly demonstrate that it was intended by Congress to apply broadly across all real estate related financial transactions involving governmental programs. Moreover, the principal author and the Congressional sponsors of Title XI were acutely aware of the banking agencies' regulatory failures in connection with the 1980s collapse of the thrift industry, including their inattention to the role played by an unregulated appraisal services industry and faulty and fraudulent appraisals which added billions of dollars to the cost of the S&L cleanup. Given this legislative history, it is inconceivable that Congress intended for these same regulatory agencies to have authority not only to rewrite the appraisal reform law but to effectively repeal it for most real estate related financial transactions, as they are attempting to do and close to doing; (See bottom of page 7 for more detail)

(4) **Subsequent to the 1994 Appraisal and Evaluation Guidelines, Congress enacted major laws that applied Title XI to federal programs that the banking agencies say they have exempted from the appraisal law:** Congress has recently enacted major laws which explicitly extend Title XI to federal housing and mortgage guaranty programs that the banking agencies say are exempt from Title XI because they are not federally related transactions. It is beyond improbable that Congress would enact laws which extended Title XI requirements to federal programs that the banking agencies' claim are not covered by Title XI if Congress didn't believe that these programs are, in fact, covered by the appraisal law. It is absurd to believe that the banking agencies have a better and more authoritative understanding of the intent of Congress when it enacted Title XI than Congress itself; (See page 11 for more detail)

(5) **The exemption provisions of the 1994 Appraisal Guidelines, which the banking agencies now claim excluded most transactions from Title XI requirements, do no such thing. A full reading of the Guidelines makes clear that at the time they were issued, the banking agencies did not exempt the government's real estate related financial transactions from Title XI's <u>enforcement</u> provisions:** The banking agencies' contention that its 1994 Appraisal and Evaluation Guidelines exempted most real estate related transactions from the entirety of Title XI is false. A complete reading of those Guidelines demonstrates clearly that it does no such thing. Apart from the fact that Title XI does not give the banking agencies any exemption authority, the most that can be argued is that the 1994 exemptions only apply to Title XI's appraiser qualifications and appraisal standards provisions (and only if the affected housing and mortgage agencies already had their own comparable appraisal requirements – which they did). The plain language of the 1994 Guidelines makes clear that the exemptions did <u>not</u> apply to Title XI's enforcement provisions (i.e., the state appraiser licensing agencies and the federal Appraisal Subcommittee) – provisions without which there is no realistic way to ensure compliance with the law's substantive requirements. They merely recognized that since these agencies had appraiser qualifications

and appraisal standards comparable to those of Title XI, requiring them to meet the Title XI provisions would be redundant. (See page 9 for more detail)

The points made in this Executive Summary are discussed below and in the pages that follow in more detail.

I. Background of the Banking Agencies' Aggressive Efforts To Restrict the Reach of Title XI

The federal bank regulatory agencies are on the verge of effectively repealing Title XI of FIRREA by taking the position that its appraisal reforms only apply to a tiny fraction of all real estate related financial transactions in which the federal government has a safety and soundness or a consumer protection responsibility. They have done so in two ways: First, by defining a key operative phrase in Title XI ("federally related transaction") in a way that dramatically shrinks the reach of the law; and Second, by approving a series of increases in the de minimus dollar threshold under which a Title XI professional appraisal of residential property is not required: from a \$50,000 threshold in 1990 to \$100,000 in 1992 and to \$250,000 in 2010 (the current threshold). An additional threshold increase to \$400,000 or \$500,000 is currently being considered by the banking agencies under the EGRPRA regulatory review process.

The FDIC appears to be the lead agency in declaring that Title XI gives the banking agencies unprecedented legal authority to unilaterally dismantle, by administrative fiat, the law they are required to administer as Congress intended. A senior representative of the FDIC told an April meeting of Association of Appraiser Regulatory Officials (AARO) that under its interpretation of the Title XI phrase, "federally related transaction", only about 10% - 12% of all governmental real estate related financial transactions are covered by the law. The FDIC representative also said that if the additional de minimus increase being considered is adopted, the 10% to 12% number would fall to about 4% of all real estate related financial transactions.

Although the conference attendees were startled by the FDIC representative's message (i.e., that their decades old interpretation of what is or is not a federally related transaction was wrong), they were told that they shouldn't be surprised by the pronouncement because the banking agencies exempted most such transactions from the jurisdiction of Title XI twenty-two years ago in the 1994 Interagency Appraisal and Evaluation Guidelines (see appendix A, exemptions 9 and 10). However, as is made clear in this paper, none of the Title XI government agency or private sector stakeholders – none – understood exemptions 9 and 10 as having the meaning and effect the FDIC now says it does. Moreover a careful and common sense reading of the 1994 Guidelines leads to an interpretation of exemptions 9 and 10 that is very different than – and inconsistent with – the FDIC's current interpretation (also explained below).

II. The de minimus dollar threshold issue

While the focus of this White Paper is on the banking agencies' improper definition of the Title XI phrase, "federally related transaction", the agencies' systematic and arbitrary increases in the dollar threshold below which appraisals are not required (and the prospect of further increases) also severely undermines the effectiveness of Title XI and, we believe, deserves the intervention of Congress. While Title XI does grant the banking agencies authority to increase the dollar threshold if they determine that an increase will not impact the safety and soundness of financial institutions, it should be self-evident that Congress never intended that authority to be exercised in a way that effectively repeals a law whose central purpose affirms and promotes the role of appraisals as the most effective method to ensure the reliability and integrity of collateral valuations for loans ultimately backed by taxpayers. If the banking agencies believe that professional appraisals of properties collateralizing millions of residential mortgage loans that are guaranteed or insured by taxpayers, are an unnecessary component of safe and sound loan underwriting, then it should ask Congress to amend Title XI in a way which explicitly gives them limitless authority to eliminate or marginalize the role of appraisals in the underwriting process. They do not now have this authority.

Given the strongly pro-appraisal policies of the government's housing and mortgage guaranty agencies and given the collapse of the housing and mortgage markets in the 1980s and much more recently, we do not believe that Congress will share the apparent view of the bank regulators that appraisals are a throw-away part of loan underwriting and grant them such authority. Our view is that the current $250,000 threshold for residential loans represents an abuse of the discretion Congress granted the banking agencies and we respectfully urge Congress to address this matter at its earliest opportunity.

III. The "federally related transaction" Definition Crisis

The banking agencies have made clear that under their restrictive interpretation of Title XI's "federally related transaction" phrase, the appraisal law does not apply to or protect any FHA or VA housing loan guaranty; any USDA rural housing program; any Fannie Mae or Freddie Mac mortgage purchase or sale; and, any mortgage origination that simply qualifies for sale to a GSE. This shocking interpretation of Title XI – which places the overwhelming majority of all residential mortgages beyond the law's protections – surfaced and became clear only recently and stunned Title XI stakeholders, in both the public and private sectors.

The banking agencies' interpretation of the "federally related transaction" phrase, means that neither Title XI's substantive appraisal provisions (i.e., appraiser qualifications and adherence to the Uniform Standards of Professional Appraisal Practice or USPAP) nor the enforcement infrastructure it established (i.e., the state appraiser licensing boards and the federal Appraisal Subcommittee) are available to users of appraisal services or to federal agencies that administer programs dependent on reliable uniform appraisals and on professional appraisers whose work is overseen by the state licensing agencies which credentialed them. Without these state and federal enforcement mechanisms, there is no realistic or cost-effective way to ensure compliance by appraisers and by users of their services with Title XI's appraisal reform provisions or with the appraisal policies of government agencies.

The improbability of the legitimacy of the banking agencies' interpretation is clearly illustrated by the following bullet points:

- **The banking agencies' interpretation is contradicted by the fact that Title XI's stakeholders both in government and in the private sector have believed for 25 years that the appraisal reform law is extremely broad-based. In other words, they are in profound disagreement with the banking agencies' interpretation.**

Federal officials whose agencies administer the nation's housing and mortgage guaranty programs have for decades operated on the basis of their belief that Title XI applies to the programs they administer. Indeed, the appraisal regulations and written policies of agencies such as FHA, VA, USDA, FHFA and the GSEs are filled with references to and reflect a dependence on Title XI, including the enforcement mechanisms it established in the form of the state appraiser licensing agencies and the federal Appraisal Subcommittee. These agencies are responsible for ensuring that valuations for federal purposes are performed by state certified or licensed appraisers who are accountable to their state licensing boards for their professionalism. Without the backup of Title XI's enforcement provisions, each of these agencies and enterprises – which rely greatly on the services of state licensed and certified appraisers – would be required to establish their own qualifications requirements for individuals who wish to provide them with collateral valuation services; to establish testing protocols to ensure that applicants meet the qualifications requirements; and, to create their own enforcement and sanctions mechanisms – functions which if not available through the Title XI structure would cost taxpayers tens or hundreds of millions of dollars to create and administer themselves.

- **The banking agencies' interpretation of their powers to restrict the reach of Title XI is sharply contradicted by the legislative history of the law and by strong indicators of Congressional intent that it should operate broadly across government housing and mortgage market programs**

The banking agencies' actions are unambiguously contrary to the legislative history of Title XI and to Congressional intent. What Congress intended as a robust appraisal reform law designed to protect broad federal programs and interests, is close to becoming a nullity.

The agencies have falsely determined that Congress intended for Title XI's appraisal reform provisions to cover only an insignificant fraction of government housing and mortgage programs – a far-fetched and even preposterous assertion given that the law was an important component of Congress's aggressive overall legislative response to the banking agencies egregious regulatory failures relative to the collapse of the S&L industry in the 1980s. One of the most serious of those regulatory failures was the banking agencies lack of attention to the flood of poor quality appraisals that were used by lenders to make thousands of bad real estate loans appear to be adequately collateralized; and, to the billions of dollars in added losses to the federal deposit insurance system caused by an unregulated appraisal services industry and by faulty and fraudulent appraisals.

The enactment of Title XI was a direct result of and reflected information gathered at more than a dozen Congressional oversight hearings which broadly examined the role of faulty real estate appraisals on a wide range of federal interests. The subject matter of these hearings involved not just the collapse of the S&L industry and the billions of dollars in losses to the FSLIC resulting from faulty and fraudulent appraisals of collateral properties but also the negative effects of poor quality appraisals on the government's home loan guaranty programs (i.e., FHA and VA) and the mortgage purchase and secondary market activities of Fannie Mae and Freddie Mac. Many other federal agency programs which rely to some extent on real property valuations were also examined during the hearings, including rural housing and multi-family programs. The provisions of Title XI were intended by its sponsors and by Congress to apply broadly to all real estate related financial transactions where the reliability of property appraisals had always been important to the mission of the agencies administering them.

Given this history, it is beyond improbable that Congress intended Title XI's appraisal reforms to only apply to an insignificant slice of federally related transactions in situations where reliable valuations of collateral property are an important component of safe and sound mortgage loan underwriting. It is equally improbable that Congress would entrust the banking agencies with carte blanch authority to dismantle the law by administrative fiat.

Importantly, since its enactment in 1989 and notwithstanding the highly restrictive interpretation of the law by the banking agencies, all Title XI stakeholders, both in government and in the private sector, have regarded the law as applying to a broad range of real estate related financial transactions in which the government has a safety and soundness or a consumer protection responsibility. This includes the entire community of professional appraisers; all the state appraiser licensing agencies; the federal Appraisal Subcommittee; the real estate, mortgage and housing industries; <u>and, critically, Congress itself</u>. This commonly held belief continued after issuance of the 1994 Interagency Guidelines which purported to exempt most real estate related financial transactions from the law; and it continues to this day.

Nevertheless, the FDIC representative's assertion at the recent AARO meeting that 85 - 90 percent or more of real estate related financial transactions are exempt from Title XI has caused great consternation and confusion at the state appraiser licensing agencies and among other Title XI stakeholders. They were also told that this pronouncement should not come as a surprise because the banking agencies exempted these transactions in the Appraisal & Evaluation Guidelines they issued in 1994 – 22 years ago.

- **The banking agencies' current explanation of what was intended by exemptions 9 and 10 in the 1994 Appraisal and Evaluation Guidelines is inconsistent with – and contrary to – the full text of the Guidelines**

The FDIC's recent explanation of the purpose and effect of exemptions 9 and 10 is inconsistent with the full text of the 1994 Guidelines as well as the text of the current Guidelines which were issued on December 2, 2010. Section VII of these Guidelines entitled "Transactions That Require Appraisals" states: "Although the Agencies' appraisal regulations exempt certain real estate related financial transactions from the appraisal requirements, **<u>most</u> real estate related financial transactions over the appraisal threshold are considered federally related transactions and, thus, require appraisals.**" (Emphasis added).

This declaration stands in stark contrast to the FDIC's current position that most transactions are not federally related transactions.

As further evidence that the banking agencies' current interpretation of "federally related transaction" is actually a reinterpretation that is clearly erroneous, consider that the commentary accompanying the 1994 and the 2010 Guidelines relating to the exemptions makes clear that they only relate to Title XI's appraiser qualifications and appraisal standards requirements if the loan guaranty agencies and the secondary market enterprises already have comparable requirements – which they did. The exemptions in the Guidelines do not create an exemption from Title XI's enforcement provisions (i.e., the state licensing agencies and the federal Appraisal Subcommittee) and were never intended to do so. A reading of the plain language of the exemption provisions of the Guidelines makes this conclusion certain:

> **"9. Transactions Insured or Guaranteed by a U.S. Government Agency or U.S. Government-Sponsored Agency**
>
> This exemption applies to transactions that are wholly or partially insured or guaranteed by a U.S. government agency or U.S. government-sponsored agency. The Agencies expect these transactions to meet all the underwriting requirements of the Federal insurer or guarantor, including its appraisal requirements, in order to receive the insurance or guarantee. (Emphasis added)
>
> **10. Transactions That Qualify for Sale to, or Meet the Appraisal Standards of, a U.S. Government Agency or U.S. Government-Sponsored Agency**
>
> This exemption applies to transactions that either (i) qualify for sale to a U.S. government agency or U.S. government-sponsored agency,[43] or (ii) involve a residential real estate transaction in which the appraisal conforms to Fannie Mae or Freddie Mac appraisal standards applicable to that category of real estate. An institution may engage in these transactions without obtaining a separate appraisal conforming to the Agencies' appraisal regulations. Given the risk to the institution that it may have to repurchase a loan that does not comply with the appraisal standards of the U.S. government agency or U.S. government-sponsored agency, the institution should have appropriate policies to confirm its compliance with the underwriting and appraisal standards of the U.S. government agency or U.S. government-sponsored agency." (Emphasis added)

It is unsurprising, therefore, that all the federal, state and private sector stakeholders understood that the so-called exemptions found in the 1994 Guidelines related only to the Title's appraiser qualifications and appraisal standards provisions based on the fact that these agencies' own appraisal requirements were comparable to those in Title XI. Applying Title XI's appraiser qualifications and appraisal standards provisions would have been redundant. None of the federal agencies believed or had reason to believe that the appraisers and appraisals utilized in connection with their programs were exempt from the enforcement authority of the state appraiser licensing agencies and the federal Appraisal Subcommittee. Nor did any of the private sector stakeholders involved in mortgage loans guaranteed or insured by government agencies or enterprises believe that the 1994 Guidelines exempted them or their transactions from the entirety of Title XI.

Title XI stakeholders understood that exemptions 9 and 10 in the Guidelines were nothing more than an acknowledgement that the FHA, VA, FHFA, USDA and the GSEs already had in place substantive appraiser qualifications and appraisal standards that were equivalent to, or strong than, those established in Title XI; and that applying Title XI's substantive requirements was unnecessary.

- **The banking agencies current interpretation of "federally related transaction" is directly contradicted by the enactment of laws subsequent to 1994 that extended Title XI to transactions the FDIC now says are outside the scope of Title XI because they are not federally related transactions**

Consider, for example, that in 2009, the Housing and Economic Recovery Act directed that "any appraiser chosen or approved to conduct" FHA appraisals must hold a state certified appraiser credential (previously, licensed appraisers were eligible to perform FHA-related valuations). It is extremely difficult to understand why Congress, in 2009, would legislate an improvement in FHA's appraisal requirements if Congress believed that 15 years earlier the banking agencies had exempted FHA's loan guaranty programs from the authority of the state licensing agencies established pursuant to Title XI to credential appraisers and oversee their professionalism; and exempted FHA's appraisers from the indirect authority of the federal Appraisal Subcommittee. Federal programs which rely on the services of state certified or licensed appraisers are tied into and depend upon Title XI (in some cases to establish appraiser qualifications and appraisal standards if the agencies don't already have them) but always in connection with the Title's enforcement mechanisms which ensure the integrity and uniformity of federally-related valuations.

Consider what <u>each</u> federal agency utilizing the services of certified and licensed appraisers would have to do if their programs were exempt from Title XI: Each agency would be forced to establish their own qualifications and standards requirements for their appraisers; each would be required to test and approve or deny eligibility to those wanting to perform appraisals for the government; each would be required to create teams of investigators to review complaints of appraiser incompetence or misconduct; and, each would have to establish their own sanctions regimes for alleged misconduct or negligence including due process protections. In short, each federal agency with a need for appraisal services would have to duplicate systems which are already in place pursuant to Title XI. This would cost taxpayers tens and possibly hundreds of millions of dollars.

Also consider that in 2010, Congress enacted Dodd-Frank which included numerous important changes to Title XI's appraiser certification and licensing system that directly impact appraisals performed for the government's principal housing and loan guaranty programs – programs which the FDIC now claims are not even subject to Title XI because they are not federally related transactions.

For example, Dodd-Frank's appraisal provisions strengthen Title XI's appraiser independence provisions by prohibiting acts and practices which seek to improperly influence an appraiser's opinion of value and by requiring that appraiser's be paid customary and reasonable fees. Dodd-Frank also amended Title XI by requiring state appraiser agencies to regulate Appraisal Management Companies (through which most appraisal engagements are ordered by mortgage lenders); by mandating that the federal Appraisal Subcommittee award grants to state licensing agencies so that they can more effectively investigate complaints filed against their appraisers; by establishing an appraisal complaint hotline to enhance the enforcement powers of state licensing agencies; and, by giving the Appraisal Subcommittee explicit authority to engage in rulemaking on issues central to the effective functioning of the system Title XI created.

<u>If Members of Congress shared the FDIC's view that only about 10% of all real estate related financial transactions are federally related transactions covered by Title XI, they never would have devoted the time and effort necessary to enact such far-reaching Title XI changes</u>.

Moreover, virtually all of the appraisal authority and requirements established by Congress in the Housing and Economic Recovery Act of 2009 and in the Dodd-Frank Act of 2010 would be a nullity if the FDIC's reinterpretation of Title XI were allowed to stand. Whose judgment should prevail on the issue of Congressional intent with respect to whether Title XI was intended to operate broadly across government programs or narrowly: Congress itself or the banking agencies? The question answers itself.

IV. Additional Points for Clarification Purposes

- Title XI was constructed in two interdependent ways to safeguard federal interests: First, it established substantive requirements to ensure appraiser competency, independence and accountability and mandated appraiser adherence to the uniform standards of professional appraisal practice (USPAP); and, second, it established an institutional framework to ensure and enforce compliance with appraiser qualifications and uniform appraisal standards. This institutional framework is composed of appraiser licensing agencies (in the 50 states, four territories and DC) which test and license professional appraisers and can sanction them based on a finding of negligence or unethical behavior; and, a federal Appraisal Subcommittee (which is a part of the Federal Financial Institutions Examination Council or FFIEC) to oversee the licensing agencies to ensure their diligence and effectiveness. Without this institutional framework, Title XI's substantive requirements would exist in a vacuum without the ability to be enforced;

- State laws establishing real estate appraiser licensing agencies pursuant to Title XI of FIRREA generally limit the authority of these agencies to "federally related transactions" performed within the state. As a result, transactions exempted from Title XI by the federal banking agencies are largely beyond the scope of the authority of most state appraiser licensing agencies and entirely beyond the scope of the authority of the federal Appraisal Subcommittee which oversees the effectiveness of the state appraiser licensing agencies. While states with laws that mandate the use of licensed or certified appraisers for all transactions within their state might be able to exercise some authority over exempted transactions, the extent of their authority over non-federally related transactions has never been tested. Moreover, if 85 – 90% of transactions occurring in a state are no longer considered federally related transactions by the banking agencies, the legislatures in these states would be tempted to amend their appraisal licensing laws to restrict the activities of their appraiser licensing agencies just to federally related transactions and pare their budgets accordingly. This is a likely scenario because the impetus to establish state appraiser licensing agencies in the first place resulted from the enactment of Title XI and the belief that the vast majority of real estate related financial transactions occurring in the states were federally related transactions. If most are now deemed not to be federally related transactions, many of these appraiser licensing agencies would be shut down or their activities substantially curtailed.

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STATEMENT OF THE

NATIONAL ASSOCIATION OF REALTORS®

SUBMITTED FOR THE RECORD TO THE

THE UNITED STATES HOUSE OF REPRESENTATIVES
FINANCIAL SERVICES COMMITTEE

HEARING TITLED

"MODERNIZING APPRAISALS: A REGULATORY REVIEW AND THE FUTURE OF THE INDUSTRY"

NOVEMBER 16, 2016

EQUAL HOUSING OPPORTUNITY

Introduction

The National Association of REALTORS® (NAR) thanks the House Financial Services Committee for holding this important hearing. Appraisals provide an independent and impartial analysis of local housing markets, and a credible opinion of the value of a house. This analysis is a critical component of the home mortgage transaction, helping to ensure the buyer is paying a fair market value for the property, and that the lender is fully informed when determining loan terms. NAR represents a wide variety of housing industry professionals, including approximately 30,000 licensed and certified appraisers, committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers. Proper regulation of the appraisal industry is necessary to ensure safety and soundness in the nation's housing market.

Federally Related Transactions

NAR firmly supports maintaining the current de minimus requirement for federally related transactions, in which real estate appraisals are required for real estate loans with a transaction value equal to or greater than $250,000. According to NAR's research, in 2015, there were 1,591,357 existing single-family homes sold for between $250,000 and $500,000. This equals about 30% of the total home sales in 2015. Compared to that number, only 632,509 existing single-family homes sold for over $500,000 in 2015. In addition, only 5 out of 180 U.S. metropolitan areas had a median existing single-family home value above $500,000. Increasing the appraisal threshold to $500,000, which some in the industry have suggested, would severely reduce the number of appraisals required in residential real estate transactions in many communities, putting into question the safety and soundness of those transactions, as well as the well-being of neighborhoods in which those loans are made.

NAR is concerned about the varying quality of valuation tools used by lenders for transactions that fall outside of the federal requirements for an appraisal. Some of the on-line automated valuation tools available today are not sophisticated enough to be relied on for an accurate valuation of real property. Should the appraisal threshold be raised, lenders relying on these estimating tools could be severely under- or over-estimating a property's value in a number of real estate transactions. NAR believes that there should be qualified appraiser oversight of all review processes that meet Uniform Standards of Professional Appraisal Practice review guidelines. Computer generated materials and check lists can complement an appraisal review, but should not act as substitutes for a licensed or certified appraiser's opinion.

Raising the appraisal threshold level would likely increase the levels of risk lending institutions have to manage. When the Government Accountability Office (GAO) investigated this issue[1], GAO found no support for raising the current threshold. Rather, GAO reported that many stakeholders supported the reduction or elimination of current threshold levels, helping to improve risk

[1] "REAL ESTATE APPRAISALS: Appraisal Subcommittee Needs to Improve Monitoring Procedures." GAO-12-147: Published: Jan 18, 2012. Publicly Released: Jan 18, 2012. *Available at* http://www.gao.gov/assets/590/587735.pdf.

management and providing better consumer protection. Increasing the appraisal threshold levels would undermine the health of the real estate lending industry as a whole.

Appraiser Qualifications

NAR firmly believes in the continuing need for competent, professional appraisers. Persons who perform appraisals of real property must be licensed or certified by their respective state regulatory agency. Appraisers follow the minimum education, experience, and examination requirements for real property appraisers to obtain a state license or certification. Appraisal competency requires a true understanding of the valuation process and is developed over time through training and experience.

In December 2011, the Appraiser Qualifications Board (AQB) adopted revisions to the *Real Property Appraiser Qualification Criteria* to require a Bachelor's degree or higher for Certified General and Certified Residential classifications. The new education requirement went into place on January 1, 2015. College degrees are costly and time-consuming. NAR is concerned that the wages earned as an appraiser are not an incentive for an individual to enter the profession after paying for a four-year college degree, especially when a graduate must do a multi-year internship that is often unpaid. The degree requirement also disadvantages workers who already have thousands of hours of appropriate on-the-job training and could be great candidates to take the certified general or certified residential exam without completing a four-year degree. The AQB should count years of experience in the appraisal profession under a trainee license to qualify for at least part of the four-year college degree requirement. Many very good existing Certified General and Certified Residential appraisers do not have four-year degrees. These same appraisers have successfully mentored many others to follow in the profession with the highest standards.

Regulatory Structure

NAR is committed to responsible valuation principles and to ensuring a regulatory framework that supports credible, independent valuations of real property because credible independent valuations of real property are critical to the health of the overall real estate industry. As such, NAR supports and promotes the mission and vision of the Appraisal Foundation[2] which promotes professionalism and ensures public trust in the valuation profession through the promulgation of the Uniform Standards of Professional Appraisal Practice (USPAP), appraiser qualifications (AQB), and guidance regarding valuation methods and techniques. NAR supports USPAP as the national valuation standard. Additionally, the NAR Code of Ethics requires REALTORS® who provide appraisal services, to conform to the standards of practice expected in that specific real estate discipline. NAR believes that appraisal standards should be uniform across the United States and territories, and does not support efforts to dilute USPAP or layer on additional sets of valuation standards.

[2] NAR is an affiliate sponsor of the Appraisal Foundation.

Federal and Conventional Programs

Over the past year, many appraisers became wary of participating in Federal Housing Administration (FHA) insured home loan transactions due to concern and confusion over appraisal requirement changes in the FHA Single Family Housing Policy Handbook. Specific rules that required appraisers to test appliances resulted in many appraisers increasing their fees for FHA appraisals. Some appraisers even stopped taking on any FHA appraisals, or asked for additional home inspections to comply with the Handbook requirements. NAR members voiced serious concern that the entire transaction had become costlier and time-consuming; hindering an FHA borrower's ability to compete in today's housing markets. In response to those concerns, FHA recently announced updates to the Handbook that clarifies this requirement. According to the new guidance, appraisers must simply note that certain appliances contributing to the market value of the property are physically present rather than requiring an appraiser to operate the appliances.

However, there are still improvements to be made in both the Handbook and FHA's general policy on appraisals. In particular, NAR has great concern over the requirement that an appraisal stays with a property for 120 days for any FHA transaction. This policy harms both buyers and sellers in rapidly changing markets, hindering economic recovery in certain neighborhoods across the country. By removing the requirement, FHA will help foster home-ownership and ensure borrowers who rely on FHA financing pay the fair and accurate market value for their home.

Recently, both Fannie Mae and Freddie Mac announced programs that would allow for the use of automated valuation tools in the place of traditional appraisals for certain mortgages. NAR is engaged with both entities on this matter and will monitor and assess these programs as they progress. NAR urges caution with regards to any programs that rely solely on automated valuations, but will not be making a definitive statement at this time on Fannie Mae and Freddie Mac's initiatives pending further review.

Conclusion

Thank you for the opportunity to submit these comments. NAR looks forward to working with committee members and the rest of Congress to maintain the safety and soundness of the appraisal industry while advancing growth in the appraisal field.

REVAA
Real Estate Valuation Advocacy Association

November 16, 2016

The Honorable Blaine Luetkemeyer
Chairman, House Subcommittee on Housing and Insurance
2129 Rayburn House Office Building
Washington, DC 20515

The Honorable Emmanuel Cleaver
Ranking Member, House Committee on Financial Services
Thomas P. O'Neill, Jr. Federal Office Building, 4340
Washington, DC 20515

Dear Chairman Luetkemeyer and Ranking Member Cleaver:

On behalf of the Appraisal Management Companies (AMCs) represented by the Real Estate Valuation Advocacy Association (REVAA) – an association of industry leading AMC's offering residential real estate valuations and services to lenders and secondary market investors including appraisals, Broker Price Opinions (BPO), and Automated Valuation Models (AVM) - please accept the following testimony for inclusion into the record of the November 16, 2016 House Financial Services: Subcommittee on Housing and Insurance hearing *"Modernizing Appraisals: A Regulatory Review and the Future of the Industry."*

AMCs play an integral role in helping to ensure the integrity, independence and efficiency of the residential mortgage process to meet the needs of consumers, lenders, appraisers and secondary market investors. They are required to strictly adhere to federal and state regulation and law in accordance with the Wall Street Reform (Dodd-Frank) and Consumer Protection Act, the Truth in Lending Act and federal Interagency Guidelines.

Decisions made by Congress and federal regulators to modernize residential appraisals are of tremendous impact to AMCs and the work they do for America's lenders.

Please find a detailed summary of AMCs positions on the following enclosed:

- AMC role in safeguarding appraisal independence
- AMC role in protecting consumers
- AMCs critical to mortgage lending and secondary markets
- Impact of Dodd Frank Act
- Nationwide state regulation of AMCs
- National AMC Registry and Fee
- AMC Perspective on the Appraiser Shortage
- Role of the Appraisal Subcommittee

REVAA welcomes participation in this, and future, discussions on appraisal related matters with the House Financial Services Committee.

AMCs Safeguard Appraisal Independence Requirements

AMCs have existed since the 1960s as valuable business partners for lenders and appraisers to meet consumer valuation needs by managing the ordering, tracking, quality control and delivery of valuation reports. In the wake of the global economic downturn of 2008 and the advent of Dodd-Frank, the role of AMCs grew to become even more critical for ensuring federally mandated appraisal independence to eliminate undue influence by separating parties with a financial interest in a mortgage loan transaction from appraiser selection and retention. AMCs deliver on Dodd-Frank's mandate every day so that no party "shall influence or attempt to influence the development, reporting, result, or review of an appraisal through coercion, extortion, collusion, compensation, inducement, intimidation, bribery, or in any other manner."

AMCs are Critical to America's Mortgage Lending and Secondary Markets.

The important role of AMCs has grown exponentially since 2010 to improve efficiency, ensure appraisal quality, eliminate fraud, reduce costs, achieve regulatory compliance, protect public safety, and provide support for a smooth, timely and responsive mortgage process for consumers and lenders. Among AMC responsibilities:

- **Ensuring** federally mandated Appraisal Independence Rules (AIR) by safeguarding against undue influence and fraud in the valuation process.
- **Maintaining** a qualified panel of licensed appraisers ready to execute lender valuation assignments.
- **Providing** quality assurance processes in the delivery of final appraisal and valuation products.
- **Complying** with federal and state laws governing valuation products and services.
- **Developing** future appraisal trainees.
- **Supporting** the obligations that states have in regulating appraisers (i.e., by reporting on appraiser violations of the USPAP and other relevant professional licensing standards).

Today, an estimated 66% of lenders now use AMCs exclusively for their facilitation of residential appraisals. The remaining one-third of lenders (primarily smaller lenders) manage their own in-house appraiser panels, many of which use their own panels which often include the use of AMCs. Among the value AMCs provide to lenders:

- **Act as a Compliance Partner for AMC Regulations** - Serve as invaluable partners for ensuring efficiency and compliance with state and federal AMC regulations.
- **Ensure Lender Compliance with Banking and Mortgage Regulations** - Support lender compliance with federal banking regulations (e.g., Fed, FDIC, OCC, CFPB) governing mortgage lending (i.e., appraisal review).
- **Help Reduce Costs & Ensure Appraiser Independence** – Help lending institutions reduce the costs of establishing and maintaining compliance programs to ensure federally mandated appraiser independence.
- **Protects Against Marketplace Disruption** - Ensures that lenders who use AMCs get their valuation work completed. If AMCs were not regulated in a state (per Dodd-Frank and AMC rules), lenders would be forced to create elaborate internal controls and firewalls that they would not have to create in other states to obtain their appraisal procurement functions on FRTs, with the least disruption to mortgage lending in the state.

AMCs Play a Vital Role in Protecting Consumers.

- **Safeguard Appraiser Independence and Protect Against Fraud** – AMCs help ensure that appraisals are completed in compliance with federal and state law and that the opinion of value was achieved by the appraiser independently, without undue influence. Prevention of coercion is critical to avoiding collusion within the valuation process and therefore potential fraud.
  - » A lack of appraiser independence led to previous housing bubbles and predatory lending. Long before the HVCC (Home Valuation Code of Conduct) and Dodd-Frank the nation had been adversely affected by prior

valuation crises in the 1930s and 1980s. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) was part of an effort to rein in abuse but was inadequate. The same independence protects consumers and lenders by providing assurance that real estate assets are correctly valued as there are reams of federal/state reports estimating the losses to the economy from valuation fraud.

» Most AMCs have systems and processes in place to:
  - Investigate appraiser concerns regarding attempts to influence valuation
  - Investigate consumer complaints regarding unprofessional conduct
  - Communicate with consumers to help educate them regarding misunderstandings of appraisal practices and/or principles

- **Help Lower Costs Associated with Borrowing** – While compliance with state and federal laws and rules is a big reason for lender use of AMCs, another is that lenders have high overhead and must compete in a competitive marketplace and the use of AMCs helps them provide the service efficiently and cost effectively to benefit the consumer while ensuring payment of Customary and Reasonable Fees to appraisers.

- **Provide Quality Controls** - AMCs employ quality control measures to ensure the integrity of a supportable, dependable and credible appraisal, which can identify mistakes and fraud in appraisal reports that protect consumers from faulty opinions of value.

- **Reduce Turnaround Times** - AMCs employ valuation experts to screen appraisal reports to identify issues early, and have a much larger success rate in resolving valuation issues without causing unnecessary delays and mitigate consumer dissatisfaction.

- **Assure that a Competent Appraiser is Selected** - Ensure only the most qualified and geographically competent appraisers are sent to a consumer's home.

- **Protect Public Safety** – Consumers are provided an extra layer of safety and protection as AMCs complete background checks of appraisers before they can be employed or empaneled. Further, AMCs continue to monitor their appraisers while they are employed or empaneled to ensure that unqualified appraisers or those that may pose a threat to public trust or safety are removed.

- **Assist Appraisers with Consumer Questions** - AMCs work with appraisers to resolve borrower questions and provide the borrower/lender an ability to submit value appeals while complying with appraiser independence.

- **Provide Customer Service Issue Resolutions** - AMCs resolve customer service escalations that are not directly related to the appraisal process through their access to lenders that the consumer may not otherwise have

The Impact of Dodd Frank

Passage of Dodd-Frank and codified in the August 2015 Final AMC Rules mandated the creation of federal rules to provide a framework for state regulation of AMCs and creation of a National AMC Registry. Federal regulation of AMCs and state regulatory programs are the responsibility of the Appraisal Subcommittee, which is governed by the Federal Financial Institutions Examination Council (CFPB, Fed Reserve, FDIC, OCC, NCUA, FHFA).

Per the now final federal interagency AMC rules, a state must adopt a compliant AMC registration and regulation program by no later than August 10, 2018. However, the final rule does not compel a state to establish an AMC registration and supervision program, and no penalty is imposed on a state that does not establish a regulatory structure for AMCs. But, failure to do so will result in AMCs being prohibited by section 1124 from providing services to lenders on Federally Regulated Transactions (FRTs).

This would cause significant disruption to lenders and consumers in a state that chose not to regulate AMCs. Furthermore, if lenders are unable to use AMCs in a state to facilitate FRTs and fulfill underwriting criteria, their available options dwindle and operational costs will dramatically increase operational costs to lenders in states that choose to "opt-out" of regulating AMCs:

- Lenders could choose to no longer offer consumers financing on FRTs that require an appraisal.

- Lenders would need to recreate internal operating and compliance infrastructure they previously shed to engage appraisers directly, while maintaining federally mandated appraisal independence requirements.

- Lenders could use small unregulated AMCs, but it will be challenging (i.e., size, tech, data security constraints).
- Lenders could use the only federally owned and controlled AMC to facilitate FRTs, but it seems unlikely since it is owned by a federally insured bank and lenders won't want to do business with a direct competitor.

REVAA Members are Now Trying to Become Regulated Nationwide

REVAA has made it a priority to ensure regulation of AMCs in each of the 50 states and five recognized territories so they comply with the mandated August 2018 deadline.

Generally, REVAA members share the sentiment in support of less state government regulation. However, Dodd-Frank has created the scenario whereby lenders and AMCs are in the precarious situation of having to advocate for at least minimal AMC regulation - despite the integral role AMCs play to safeguard appraiser independence and protect consumer safety and the investments made in mortgage transactions - to avoid what would without question be a massive disruption in the residential mortgage market that would result in negative consequences to consumers and lenders in Federally Related Transactions.

As a regulated entity, our simple request is that AMCs be treated fairly and respectfully as a co-licensee by their regulator in each jurisdiction. AMC regulation does not need not be burdensome, especially if the regulation is implemented using the minimum standards set out in the Final Rule.

We've been actively working with the states in concert with stakeholder groups to achieve consensus on the introduction and passage of legislation that complies with the minimum standards set out in the final rule. As of November 16, 2016, 40 states have passed AMC licensing programs (three of which are still working on promulgating required administrative rules). For states with existing AMC regulatory schemes, nominal legislative changes are typically required to become compliant with the federal AMC rules.

REVAA continues to push ahead on passing AMC legislation in the remaining 10 states and five U.S. jurisdictions by the August 2018 deadline. The overall effort to have to advocate for our own state regulation has been exceedingly costly, burdensome and resource intensive, which could have been avoided had the regulation of AMCs been made mandatory, not voluntary to ensure national consistency and efficiency.

National AMC Registry and Fee/Rising Compliance Costs

Post Dodd-Frank, the cost of compliance for individual AMCs has grown exponentially to accommodate state regulatory schemes, audits, staff and other resources needed to comply. Generally, most AMCs have a business model based on a high volume of transactions and operate within a highly competitive marketplace, which strains operating margins. Like independent fee appraisers and most regulated businesses, continually increasing financial strain is being applied by ever growing compliance requirements as well as state licensing and administrative fees across all jurisdictions. In addition, a lack of consistency in AMC regulation between states further complicates matters and increases cost. On average, for each mid to large AMC, this cost annually is now near $300,000 - $400,000.

Additionally, the implementation of the Dodd-Frank mandated AMC National Registry is estimated to cost each AMC anywhere from tens of thousands to hundreds of thousands of dollars each year. For a mid-large size AMC, these fees will likely be an additional $150,000-$250,000 each/per year. AMCs do appreciate the deliberate attempt to minimize the impacts by pursuing the minimum requirements as outlined in statute.

However, AMCs are typically small businesses with razor thin operating margins. Without question, the AMC National Registry Fee will have a substantial financial effect on AMCs regardless of their size or legal entity, including forcing some out of business and hindering the likelihood of new AMCs entering the marketplace due to the high cost of regulation and fees.

Many industries are regulated and assessed fees, and despite those regulations and fees, industries adapt to survive. AMCs will continue to evolve to meet the needs of America's home buyers, lenders and appraisers, but the way the AMC industry operates may be different tomorrow, shaped in part by the decisions made and the regulations implemented today.

AMC Perspective on the "Appraiser Shortage" – An Even Bigger Concern Looms

REVAA members share concern about current appraisal turn times and the associated rising costs.

Based on our analysis of available demographic and industry data, AMCs fear the current shortage of appraisers does exist and may be worse than forecasted. For example, often excluded from consideration is the number of Certified Appraisers who maintain an active credential but do not actively practice in the field. While on paper there may be an estimated 80,000-90,000 active residential appraisers, a significant percentage may work for lenders, AMCs, appraisal firms, government and others but are not actually appraising residential properties in the field. The shortage of appraisers may also be exacerbated by other factors such as accounting for full vs. part-time appraisers and the retirement wave of the nation's Baby Boomers, as has long been forecasted.

While reasonable people may disagree as to whether there is or is not indeed a current shortage of residential real estate appraisers or just short-term supply and demand anomalies at play, demographic data makes it disturbingly clear that there is currently no "next generation" of residential real estate appraiser in the pipeline to replace retiring workers.

The lack of a next generation of appraiser is of critical concern for REVAA members who are passionate about the future of the industry. AMCs have chosen to take an active role in helping to recruit, train and work with trainees – the first step in becoming an appraiser. Irrespective of the coming changes to be made by the AQB, and possibly adopted by the states, the critical mandate to maintain the public's trust in appraisers is absolute. REVAA supports creativity and modernization, but only so long as these changes do not diminish the integrity, professionalism and public trust in appraisers.

In its October 2015, white paper *"Building the Future: Ideas for Attracting the Next Generation of Residential Property Appraisers,"* and multiple submissions to the Appraiser Qualifications Board in its current review process, REVAA has identified ideas for public and private sector industry stakeholders (lenders, regulators, appraisers) to identify solutions for the recruitment and training of future appraiser trainees, including:

- **AMCs to Provide New Appraiser Training and Relieve the Training Burden on Supervisory Appraisers** – To help address individual appraiser concerns about the burden of being a supervisory appraiser to train trainees, REVAA members plan to broaden their role as a supervisory appraiser. We are seeking to create a uniform AMC trainee program to help connect aspiring appraisers with a greater variety of business that can provide them with high-quality field experience. AMCs can expose trainees to a higher volume of assignments, greater diversity in assignments, and the full breadth of current industry challenges and responses.

- **Lessen Restrictions on Trainee Inspections** – The AQB Criteria already allow supervisors to decide when a trainee has the competency to perform inspections on their own. But some states and many lenders put limitations on that, requiring supervisors to inspect all properties with the trainees for extended time frames or for the entire time until the new appraiser becomes Certified. A defined program that begins with the supervisor inspecting all properties with the trainee, but then progresses to further stages as competency is developed would be beneficial. That would allow the trainee, once competency has been developed, to inspect properties on their own while still completing the appraisal under the supervision of their mentor.

- **Offer a Testing Option as an Experience Alternative** – Allow aspiring appraisers to pass a comprehensive technical examination in lieu of satisfying all or part of the current professional experience requirement. Many professions (e.g., accountants, lawyers) utilize a demanding and highly specialized exam to gauge entrants' readiness and level of training, and this model could be successfully leveraged with prospective appraisers. After a student graduates from college with a four-year degree, or after he or she graduates and completes a specified minimum time in a professional internship, an "Appraisal Exam" could be used to streamline the path to becoming a credentialed appraiser.

- **Offer a Testing Option as an Education Alternative** – Create a non-degree path that will allow prospective appraisers to pass a comprehensive technical examination in lieu of satisfying the college degree requirement for an appraiser license or certification. This will ensure that competent individuals without the means to attain a two-year or four-year college degree still could become an appraiser via hard work, comprehensive training and rigorous testing.

- **Create a Program for America's Honorably Discharged Veterans** - As of 2015, there were more than 21.2 million veterans of which about 12.3 million served in the period ranging from the Gulf War (1990- 2001) to about 2015. What this means, conservatively, is that there is a pool of at least 12.3 million veterans who could consider becoming appraisers, the clear majority of whom bravely served their country and would in most instances likely be well suited to become an appraiser.

  Create incentives for encouraging honorably discharged veterans to enter the appraiser profession. One idea would be to amend the Criteria to include the acceptance of military coursework and experience on a veteran's Joint Services Transcript (JST) to meet the appraiser educational content and potentially experience requirements; again, we would propose allowing 50 percent of those hours earned relative to educational content area to be applied toward experience hours. The JST is an academically accepted document approved by the American Council on Education (ACE) to validate a service member's military occupational experience and training along with the corresponding ACE college credit recommendations.

  Most states provide varying degrees of accommodation to honorably discharged veterans ranging from expedited licensing, to reduced or waived fees and stipends in a wide array of professions. We encouraged the AQB to recommend that states enact laws and rules to provide for expedited licensing and reduced or waived fees for veterans, as well as AMCs that can provide proof they employ or have a certain number or percentage of veterans on their appraiser panels.

The Role of the Appraisal Subcommittee

REVAA members are not regulated by the ASC, we are regulated in the states by designated appraisal agencies who are regulated by the ASC. With the rapidly approaching final AMC Registry rules and the August 2018 deadline to have federally compliant AMC rules in place, the nature of the relationship between ASC and AMCs is going to change exponentially, as will the AMCs new oversight of state AMC regulatory programs. Over the years, REVAA and its members have had a positive working relationship with the ASC and its staff in the contemplation of rules and policies that impact AMCs.

Thank you for considering our comments. Please do not hesitate to contact me with questions.

Respectfully,

Mark A. Schiffman

Mark Schiffman
Executive Director

REVAA Member Companies:

Accurate Group
Appraiservendor.com
Asset Valuation & Marketing
Assurant Specialty Property
Axios
Clear Capital
CoreLogic
eMortgage Logic
Fidelity Residential Solutions
Independent Settlement Services
LRES
MCS Valuations
Nations Valuation Services
PCV Murcor
Pro Teck
ServiceLink
SingleSource
STARS
Stewart Lender Services
StreetLinks
SWBC Lending Solutions
TitleSource
The William Fall Group
XOME

House Committee on Financial Services

Hearing: "Modernizing Appraisals: A Regulatory Review and the Future of the Industry"

November 16, 2016

Questions for the Record from U.S. Representative Ed Royce (R-Calif.)

Mr. Ed Brady, Chairman of the Board, National Association of Home Builders

Under the FHA's recent guidance on PACE loans, an appraiser must analyze the impact of PACE-related improvements on the value of a home if the obligation is staying with the property. What's your assessment of the current ability of appraisers to value PACE home modifications? What's the impact of this development on appraisal costs and ability of sellers to enter the market?

NAHB Response:

NAHB is a long-standing proponent of energy efficient new homes and energy efficient retrofits in existing homes that offer home owners the benefit of lower utility payments and contribute to efforts to reduce energy consumption.

NAHB believes that substantial efforts should be made to obtain an accurate assessment of the subject home's value and to ensure that the liens on the property do not exceed that value. PACE assessments should be carefully calibrated to the value of the property but it would be imprudent for programs to allow assessments that, when combined with other liens, exceed the estimated value of the property.

NAHB continues to work with the appraisal industry to improve the ability of appraisers to value energy efficient upgrades. However, there remains confusion about accounting for energy efficient and other "green" features in new and existing properties. To address these impediments, the Appraisal Institute developed the Residential Green and Energy Efficient Addendum to help capture the data for these features and incorporate the information into their analysis. Additionally, the Appraisal Foundation has taken steps to improve appraisers understanding of valuing green features by developing Valuation Advisories to provide appraisers information on how to identify green features, how to determine their relevancy, how to effectively utilize research and analysis, and how to account for green features in the three approaches to value (sales comparison, cost and income).

NAHB will continue working with the Appraisal Institute and the Appraisal Foundation to update the information and keep these documents relevant for a market segment that is growing and constantly changing.

NAHB believes it is important to support initiatives, such as PACE, that seek to finance energy efficient and renewable retrofits for residential and commercial properties. However, NAHB is concerned about the potential negative impact of first-lien PACE programs on the functioning of the housing finance system.

NAHB believes that in order to expand the use of PACE financing to fund energy improvements, PACE programs should waive the superior lien position granted them through the treatment of PACE assessments as tax liens. Unless wavier of first-lien status is established as a best practice for PACE programs, this form of funding will fail to fulfill its potential role in the financing of energy improvements.

Detailed information on outstanding PACE liens must be readily available throughout the mortgage lending community in order to achieve broader use of PACE financing. Similarly, thorough and accurate data on energy improvements must be available and utilized by appraisers in order to accurately determine the value of energy improvements.

THE APPRAISAL FOUNDATION
Authorized by Congress as the Source of Appraisal Standards and Appraiser Qualifications

January 11, 2017

The Honorable Ed Royce
U.S. House of Representatives
2310 Rayburn House Office Building
Washington, DC 20515

Dear Congressman Royce:

This is in response to a question you raised regarding my testimony before the Subcommittee on Housing and Insurance of the House Committee on Financial Services at its November 16, 2016 hearing entitled "Modernizing Appraisals: A Regulatory Review and the Future of the Industry."

Specifically, you asked:

> *You testified that "output is only as good as its input" when it comes to automated valuation models (AVMs). How can Congress improve the input? What are the main hurdles in this arena?*

As far as how Congress can improve the quality of AVMs, the *Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* contained a provision directing the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the National Credit Union Administration Board, the Federal Housing Finance Agency, and the Consumer Financial Protection Bureau to promulgate regulations to implement quality control standards for AVMs (attachment #1). Unfortunately, we are unaware of any action taken to date in this regard.

There are many issues with the accuracy of AVMs. Before examining the veracity of comparable market data, the first concern is the accuracy of the information for the *subject property* itself. Homes are constantly being updated, renovated, enlarged, etc. Obviously, the best comparable market data in the world is meaningless if it is being considered in light of a property whose physical characteristics are not accurately identified in public records. Assuming the information about the subject property *is* accurate, questions regarding the available comparable data remain: How relevant are the properties selected to the subject property? How "fresh" is the data, particularly in dynamic real estate markets? Of what use are AVMs in non-homogenous housing markets? There are markets where the value of properties on the same street may differ dramatically because of the varying views they afford. Properties may be worth more or less based on which side of the street and how far up or down the block they are located.

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The Honorable Ed Royce
U.S. House of Representatives
January 11, 2017
Page Two

I have taken the liberty of attaching an article about this issue from the *Toronto Globe and Mail* that illustrates the potential shortcomings of AVMs (attachment #2)

I hope you find the above information to be responsive to your inquiry. If you have any questions or need additional information, please feel free to contact me at 202-624-3040 or via e-mail at david@valuation.org.

Sincerely,

David S. Bunton
President

Attachments

Attachment #1

Dodd-Frank Wall Street Reform and Consumer Protection Act

SECTION 1473:

Automated valuation models

Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (12 U.S.C. 3331 et seq.), as amended by this section, is amended by adding at the end the following new section (and amending the table of contents accordingly):

1125.

Automated valuation models used to estimate collateral value for mortgage lending purposes

(a) In general

Automated valuation models shall adhere to quality control standards designed to—

(1) ensure a high level of confidence in the estimates produced by automated valuation models;

(2) protect against the manipulation of data;

(3) seek to avoid conflicts of interest;

(4) require random sample testing and reviews; and

(5) account for any other such factor that the agencies listed in subsection (b) determine to be appropriate.

(b) Adoption of regulations

The Board, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the National Credit Union Administration Board, the Federal Housing Finance Agency, and the Bureau of Consumer Financial Protection, in consultation with the staff of the Appraisal Subcommittee and the Appraisal Standards Board of the Appraisal Foundation, shall promulgate regulations to implement the quality control standards required under this section.

(c) Enforcement

Compliance with regulations issued under this subsection shall be enforced by—

(1) with respect to a financial institution, or subsidiary owned and controlled by a financial institution and regulated by a Federal financial institution regulatory agency, the Federal financial institution regulatory agency that acts as the primary Federal supervisor of such financial institution or subsidiary; and

(2) with respect to other participants in the market for appraisals of 1-to-4 unit single family residential real estate, the Federal Trade Commission, the Bureau of Consumer Financial Protection, and a State attorney general.

(d) Automated valuation model defined

For purposes of this section, the term automated valuation model means any computerized model used by mortgage originators and secondary market issuers to determine the collateral worth of a mortgage secured by a consumer's principal dwelling.

Attachment #2

THE MARKET

Potentially flawed data used by banks and lenders bump up house prices

GRANT ROBERTSON AND TARA PERKINS
The Globe and Mail
Last updated Thursday, Oct. 11, 2012 6:30PM EDT

A house for sale in Toronto. (Galit Rodan/The Globe and Mail)

Flaws in a national databank that helps determine the value of houses across Canada have helped fuel inflation in home prices, putting mortgage lenders and borrowers at greater risk, key players in the housing sector have warned.

Documents obtained by The Globe and Mail detailing confidential statements from banks, appraisers and mortgage insurers show rising worry over the use of a database operated by the Canada Mortgage and Housing Corporation (CMHC). The documents suggest the data are flawed and help push home prices up.

Introduced in 1996 as a way for the CMHC, banks and other lenders to quickly and inexpensively determine how much money can be lent against a residential property, the database known as Emili is relied upon too heavily by lenders, the documents suggest.

Emili is an automated system that uses figures such as recent sales of nearby homes to gauge values, without sending an actual appraiser to the address. However, the potential margin of error in calculations may pose significant problems. For home buyers, or homeowners with home-equity lines of credit, an inaccurate valuation by the database could allow them to overpay or borrow much too heavily for the home, industry members argue.

For banks, it could mean the collateral they have against the mortgage is not worth as much as believed.

"Although it provides very rapid responses, this automated approval system has significant shortcomings," says one industry respondent in the documents, which were obtained by The Globe and Mail through access to information requests.

Because the database does not evaluate a specific property, but uses generalities to determine the risk level of a mortgage, "CMHC insured loans are often granted without truly taking into account the property's market value," the respondent says. "This poses a real danger of altering housing market data."

CMHC is the largest mortgage insurer in the country. The documents, from May, were part of a process by the federal banking regulator, the Office of the Superintendent of Financial Institutions (OSFI), to determine whether Canada's mortgage lending rules needed to be tightened.

Though it is not possible to know who is responsible for each comment, since the names of each industry player are redacted to comply with privacy laws, numerous parties flagged concerns about the accuracy of Emili data in gauging home values. Groups who responded to the call for comments include the country's major banks, real estate associations, representatives of the appraisal industry, mortgage insurers, and mortgage brokers.

OSFI advised banks this summer to take a closer look at how they determine housing values, and to make more effort to do more in-person appraisals. However, when those new guidelines were announced, there was no indication of the extent of the concerns raised in private by industry, and the heightened level of concern over the accuracy of Emili data.

Known as an automated value model (AVM), Emili is used to estimate whether a mortgage or a refinancing is risky or not. When financial players, including CMHC, use Emili, they submit a proposed value to the database, which then responds by saying whether the value fits within the range for that community or not. However, the database can not tell whether the actual property is worth that much.

"It allows people to pay too much for a property," Rick Sieb, president of Intercity Appraisals Ltd. in Vancouver, said in an interview. "If the property is worth $300, and somebody comes through and the realtor has convinced him to pay $330, so he's 10 per cent out, and they submit it through Emili or another AVM, it will just say 'yeah, that's fine for that area," Mr. Sieb said. "So the lender still lends the money, the guy still buys it, and the only person hurt in the whole deal is the person who paid too much."

The Canadian housing market has been on a tear for much of the past decade but is now showing signs of petering out. During that time, consumers took on record-high levels of mortgage debt, a situation that has troubled Finance Minister Jim Flaherty, who sought to cool the housing market to prevent it from overheating any more and ultimately crashing. His goal has been to steer it towards a so-called soft landing. The latest market data suggest house sales have been falling since he tightened the rules.

During a hot housing market, a wider margin of error on estimated values was less of a concern, since there is smaller likelihood a mortgage or loan refinancing will end up under water. But if the market starts to fall, as some economists expect, the accuracy of appraisals becomes paramount. When a lender is forced to liquidate a home in the event of a default, it could incur a loss. In the case of CMHC, the federal government would be left picking up the tab.

Automated systems such as CMHC's Emili emerged because they are a fast and inexpensive way to gauge the value of a property, instead of paying for an appraiser. When CMHC launched Emili, it said the move would move "application approval times from days to seconds." Emili is also used by banks on mortgages where the down payment is over 20 per cent.

Asked about the documents, a spokesperson for the CMHC said in an e-mailed statement on Wednesday that the corporation uses appraisals "where appropriate." The spokesperson added that Emili "relies on a number of different factors and models beyond home resale data" to determine risk, but did not elaborate.

The documents also suggest blunt estimates on home valuations may have resulted in higher CMHC premiums paid by consumers on insured mortgages.

Questions for the Record
Ranking Member Maxine Waters (D-CA)
FSC Housing and Insurance Subcommittee Hearing Entitled: "Modernizing Appraisals: A Regulatory Review and the Future of the Industry"
Date of Hearing: November 16, 2016

Questions for Jennifer Wagner, Mountain State Justice, Inc.

1. Please elaborate on your observation that inflated appraisals significantly contributed to the financial crisis. How did inflated appraisals play a role in the explosion of foreclosures?

Response: As set forth more extensively in my written testimony, it is well-recognized that the financial crisis was caused largely by a predatory mortgage market that trapped borrowers in home-secured loans that they could not afford and that far exceeded the true market value of the homes. The related housing bubble was in large part artificially created through inflated appraisals, obtained from appraisers who were pressured by lenders to return extremely high values on their appraisals. Based on these falsely inflated appraisals, unscrupulous mortgage lenders and brokers were able to make increasingly large home-secured loans—which resulted in higher fees for them. Often these loans were refinancing transactions, in which the broker or lender consolidated unsecured debts or provided cash out of the transaction without the borrower's knowledge or request, solely to increase the loan amount up to the inflated appraised value, and thus increase the fees paid to the originator. Many of these loans were marketed to subprime and unsophisticated borrowers, and had features that would cause payments to explode after a few years. When borrowers began to struggle with their payments, they were trapped—they could not refinance or sell because the loans so exceeded the market value of the properties. The only option left was foreclosure, and millions resulted. In this scheme, only the originating lender and broker won, while homeowners, communities, and downstream investors all ultimately bore the cost of unnecessary foreclosures.

The inflated appraisals resulted from substantial pressure from mortgage lenders across the country to increase appraised values to enable them to make larger loans. The market forces resulted in some appraisers across the nation actively engaging in fraudulent schemes. Some of these appraisers ultimately were convicted of crimes, but many were not. These appraisers received kickbacks or payoffs to inflate home values to enable flipping and other predatory lending schemes. Many more appraisers, however, were subject to subtle and explicit pressure to increase home values on their appraisals to meet high target values or otherwise be blacklisted by the mortgage companies. Appraisers faced the impossible choice of either providing the value that their customer—the lender—wanted, or lose their livelihood and career. For this reason, thousands of appraisers petitioned Congress to intervene and protect appraiser independence in the years preceding the market collapse, as referenced in my written testimony. As the number of signatories to this petition demonstrates, this problem was endemic to the mortgage market nationwide, and not just the result of a few bad actors in limited locales. And as the result of these pressures, and the resulting trap for homeowners, millions of homes were ultimately lost to foreclosure, destabilizing the entire financial marketplace.

2. Please elaborate on your comments regarding whether an appeal process could ever be appropriate, and if so, what factors should be taken under consideration in developing such a process.

Response: While an appeal process may be reasonable under extremely limited circumstances, this can be addressed through internal guidelines and processes for lenders and investors. As I've heard from many appraisers, permitting appraisal appeals creates a significant risk that the process would be subverted to allow builders, buyers, sellers, and lenders to pressure appraisers to increase the appraised values in order to satisfy an appeal and meet a target value. This is exactly the type of conduct that led to the inflated and false valuations that preceded the foreclosure crisis. However, it may potentially be appropriate under very limited circumstances to permit a lender to seek a second opinion, to request additional comparables, or to correct a typographical error if a defect is noted in the original appraisal by a qualified reviewer—and this is typically already permitted. Substantial safeguards are necessary, however, to protect appraisers from retribution or pressure in relationship to this process. However, such a process need not be legislatively formalized and is appropriately managed through the existing appraiser independence structure.

3. Should appraisers be provided any flexibility in making their decisions? Can we trust appraisers to make qualified and well-formed decisions?

Response: I have the utmost respect for appraisers, who go through rigorous training and apprenticeship to become qualified professionals in their field. The existing structure of appraisal independence promotes appraiser flexibility, by allowing appraisers to make their own independent judgments regarding the true market value of properties insulated from pressure from outside forces. Similarly, the use of appraisals by licensed appraisers, rather than automated valuation methods, permits appropriate flexibility to address the true condition, neighborhood, and ultimate value of a home. Appraisers are highly trained and knowledgeable individuals who consider and weigh a multitude of factors to reach their independent judgment of market value. All of this involves considerable discretion and flexibility. By supporting appraiser independence, appraisers are provided the flexibility that they need to make qualified and well-formed decisions.