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

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**Before the Subcommittee on Housing and Insurance**

**House Committee on Financial Services**

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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.<sup>1</sup> The long-term trend is one of decline in the number of licensed and certified real estate

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<sup>1</sup> 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<sup>2</sup>.

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<sup>3</sup>) over which it presides, and by allowing state and federal agencies to

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<sup>2</sup> 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.

<sup>3</sup> 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.<sup>4</sup> 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.<sup>5</sup>

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.<sup>6</sup>

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<sup>4</sup> “Fifth Exposure Draft of Proposed Revisions to the *Real Property Appraiser Qualification Criteria*” October 27, 2011

<sup>5</sup> <http://www.appraisalinstitute.org/ano/ai-report-analyzes-state-rules-on-appraiser-background-checks/>

<sup>6</sup> “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/Service's 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<sup>7</sup>.

### 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.

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<sup>7</sup> Available at [http://www.appraisalinstitute.org/assets/1/7/Appraisal\\_Threshold\\_Levels\\_Survey.pdf](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.

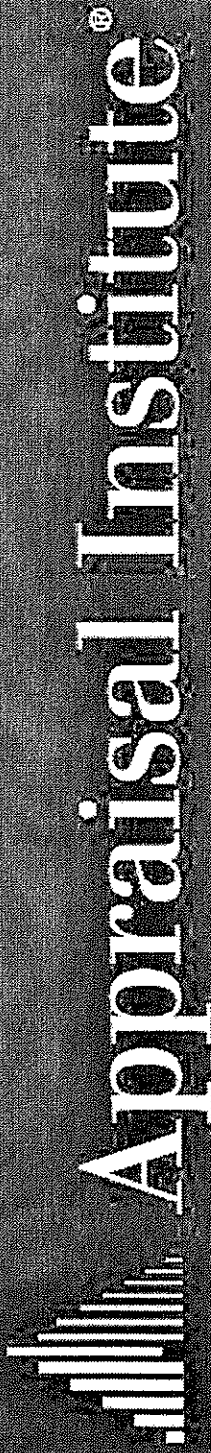
7. **Protect and maintain Dodd-Frank Act, Section 1472, appraisal independence requirements that prohibit coercion and intimidation of appraisers with the full weight of the Truth in Lending Act enforcement provisions.**

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.



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# U.S. Appraiser Population Estimates 2006 – 2016, As of June 30, 2016

# U.S. Appraiser Population

## As of June 30, 2016



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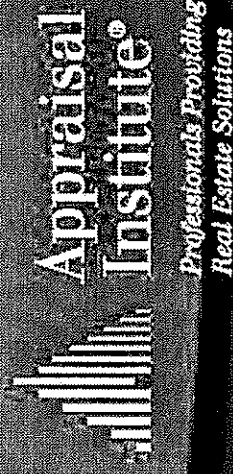
## About the Appraisal Institute

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



## 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

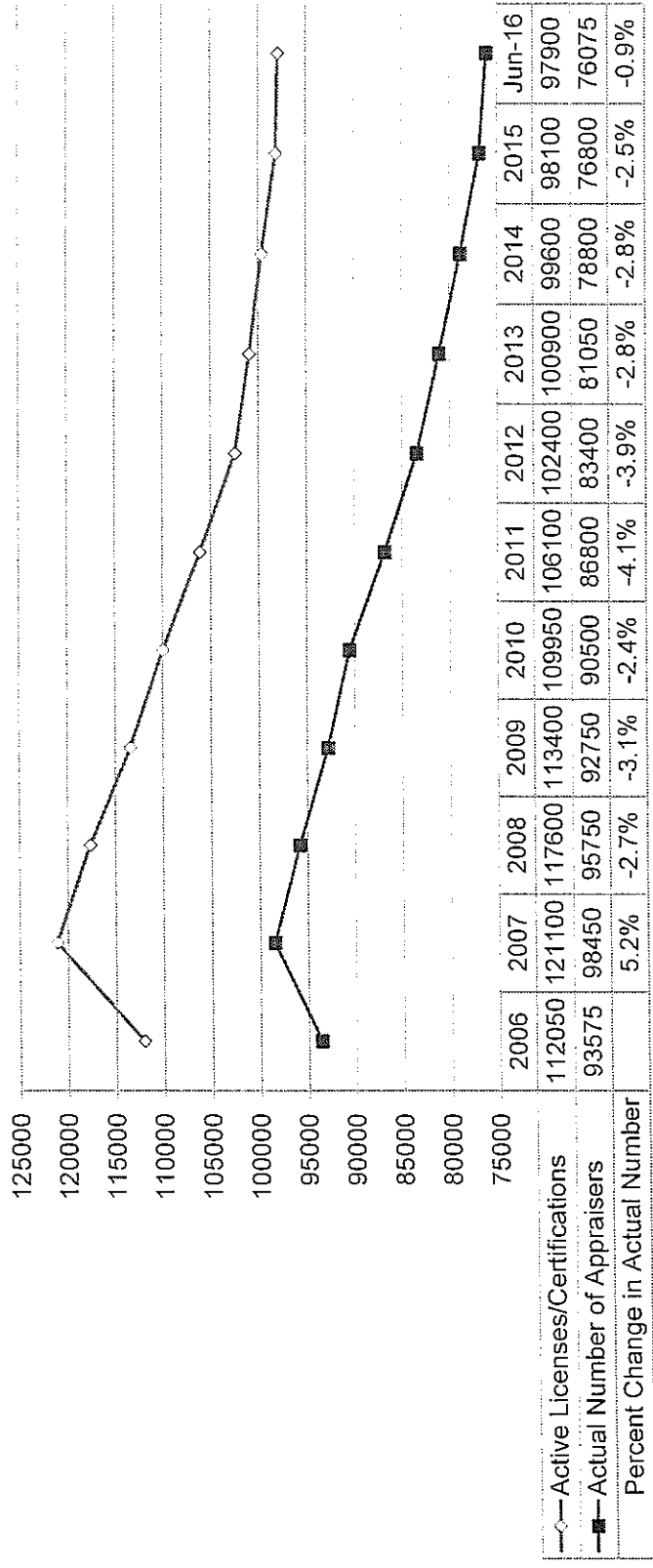
- The Appraisal Institute has analyzed ASC National Registry data since 2006 using consistent methodology. The long-term trend is one of decline in the number of licensed and certified real estate appraisers in the U.S., with decreases of nearly 3.0 percent annually. (As of June 2016, the total number 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

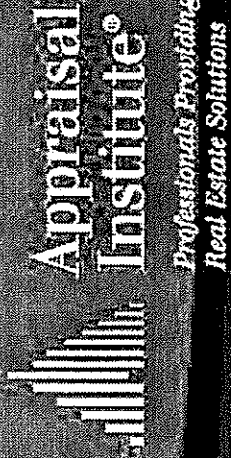
**Total Licenses, Certifications, and Number of Appraisers**



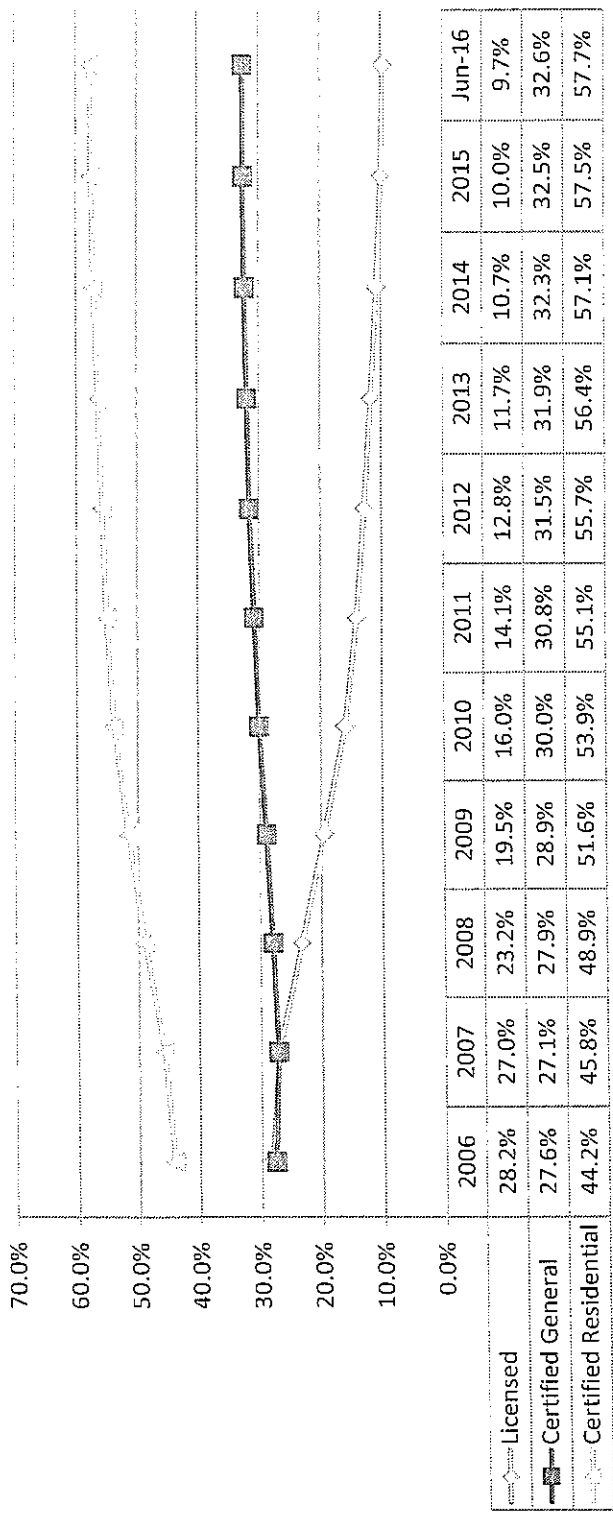
As of June 30, 2016, the total number of real estate appraiser licenses/certifications decreased by 0.2 percent from year-end 2015. Comparatively, the actual number of active appraisers decreased 0.9 percent for the same period. As of June 30, 2016, the actual number of appraisers decreased 22.7 percent from the peak year-end 2007 level. 5

# U.S. Appraiser Population

## As of June 30, 2016



Proportion of U.S. Appraisers Licensed or Certified



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.

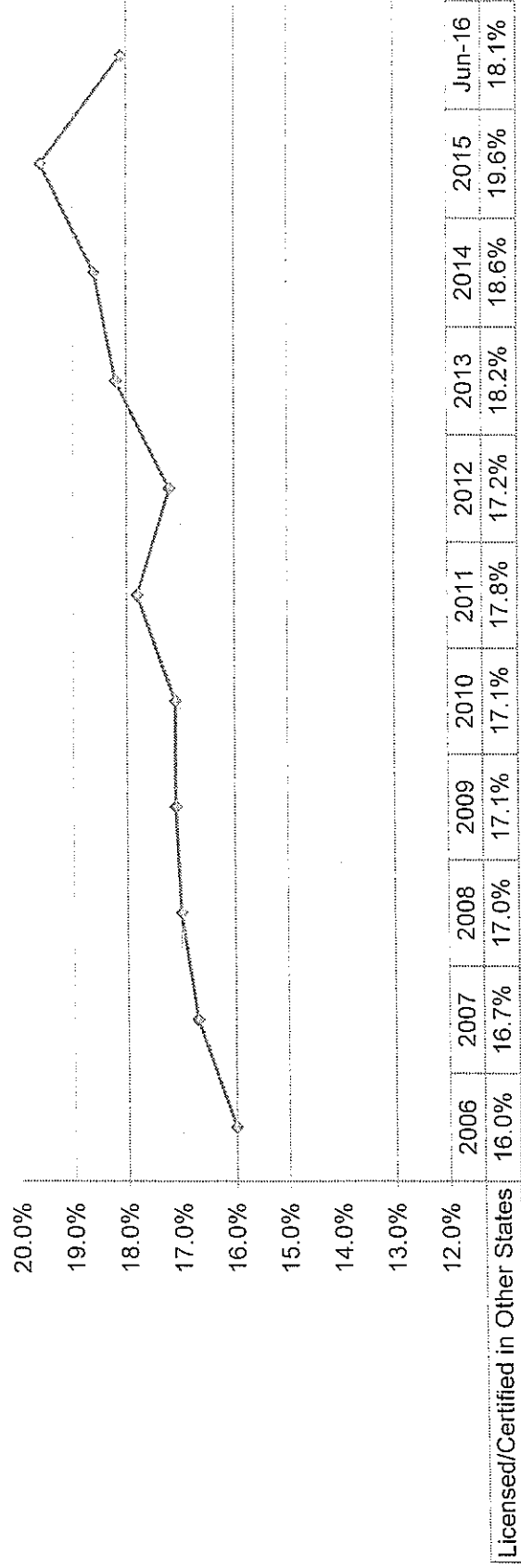
# U.S. Appraiser Population

## As of June 30, 2016



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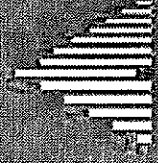
### Proportion of U.S. Appraisers Licensed or Certified in Multiple States



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