Written Statement of William F. Kidwell, Jr.
President – IMPACT Mortgage Management Advocacy and Advisory Group (IMMAAG)

"Appraisal Oversight: The Regulatory Impact on Consumers and Businesses"

Hearing before the House Financial Services Committee
Subcommittee on Housing and Community Opportunity
Thursday, June 28, 2012

Chairwoman Biggert, Ranking Member Gutierrez and Members of the Subcommittee, the following statement is offered for the record and I thank you for the opportunity to submit the statement. The thousands of state licensed mortgage loan originators not directly represented at today's important hearing depend on **IMMAAG**[1] to provide them information and occasionally to speak for them. Those professionals are central to the Congress's stated desired solutions to make the mortgage delivery processes more efficient, simpler, clearer and understandable to consumers. Today's hearing is particularly relevant to those goals in as much as the subject stands as an icon for how not to oversee market activities.

Somewhere over time it seems that the idea of why appraisals are needed has been lost. The fact is that the value of any asset is determined by the price a willing buyer pays a willing seller in an arm's length sales transaction. The idea of appraisals was borne to assist buyers and sellers with an estimate of what a fair value might be. As it relates to real property, primarily due to the financial size of the transaction and the fact that most buyers could not pay cash for the home they wanted to purchase, lenders began asking for appraisals to determine the likelihood that the amount loaned could be recovered by the sale of the underlying collateral if the even to occurred that the borrower no longer paid. Then as it became apparent that homes were investments with appreciating value which created paper equity but not liquidity, the appraisal became a method to value the asset so an owner could exchange paper equity for cash or access to a credit facility to increase liquidity.

So, there are actually two different reasons for an appraisal to be desired and each of those reasons drives a different set of expectations and motivations and needs. In the first, the purchase

[1] IMMAAG is a Colorado for profit information company founded in 2008 to provide the tens of thousands of small and independent mortgage brokers and originators a clearing house and information source regarding legislative and regulatory activity affecting their business and customers and with 2,900% growth in registered users since January 2010 has evolved into a center for advocating their common causes.

of a home, the seller is interested in an appraised value that supports the asking price. It would be naïve to believe the seller wants a lower value when trying to sell. On the other hand the buyer, even though few act this way, really wants a value that is as low as possible, but buyers generally operate as though they simply want a value that supports their emotional desire to buy a home. In the sales transactions, everything else being equal the buyer stands mostly on the sidelines with respect to the appraisal process and valuation. The lender simply wants accuracy so they are confident that the loan to value they believe they have will be adequate to recover the loan balance and costs associated with recovery.

On the other hand, the majority of appraisal transactions today do not support a purchase / sale. In fact, based on the Mortgage Banker Association's most recent report, refinances comprise almost 80% of the weekly applications for mortgages. In a refinance there are only two participants and their objectives are not congruent. The borrower wants the highest appraised value possible and the lender continues to want accuracy. This is a pure financial transaction, not a real estate transaction. I point this out because on today's panel the subcommittee will hear from a trade association representing the real estate community, but will take no testimony from state licensed mortgage brokers who represent a material portion of the delivery process affecting this huge segment of the transactions requiring appraisal.

The committee is seeking answers to the regulatory impact of appraisal oversight on consumers and business and will not have the advantage of hearing from the professionals who live and work in the local market and must process the transactions which have been negatively affected by reactions based on misinformation and misunderstanding.

Possibly more than any single change, the unilateral action taken by then New York State Attorney General Andrew Cuomo to threaten a law suit against Fannie Mae and Freddie Mac which resulted in a negotiated settlement leading to the Home Valuation Code of Conduct has harmed the housing market, cost consumers the loss of paper equity and net worth to the tune of trillions of dollars and has resulted in a process that has become imbedded so deeply that even when the Dodd Frank Act terminated the policy, the FHFA and FHA refused to change their HVCC inspired policies.

It is one thing for oversight when there is proof of harm, inefficiency or ineffectiveness. It is another thing entirely for powerful people to use their position to unilaterally influence industry based on anecdotal information and unsupported allegations. For all intents and purposes it is this cause that has led to existing appraisal processes which not only harm consumers through artificial value suppression, but harms the appraisers it ostensibly was designed to protect.

The Home Valuation Code of Conduct was a draconian flexing of the muscles of a single state's attorney general. It was so effective in changing the landscape that even after the Congress terminated it through the passage of the Dodd Frank Act, FHFA and FHA refuse to change the policies implemented specifically to support HVCC.

To address the committee's questions I will simply bullet point some of the impact of the regulatory oversight of the appraisal process. Unfortunately, with the exception of elevating the public awareness one power oriented official's stature the recent misdirected actions with respect to appraisals has produced only negative results:

Fraud: A driving reason for HVCC and resulting regulation is to reduce valuation fraud. According to MARI reports since HVCC's inception valuation fraud, to the extent it can be truly measured or estimated has not improved.

Transportability: One of the elements of the Dodd Frank Act in Section 1472(h) directed the regulators to insure appraisal transportability between lenders. This aspect of the law continues to be ignored and has not been addressed to date by regulation and the result is to make mortgage delivery inefficient, delay closings and increase consumer costs because generally while lenders pay lip service, transportability is not a widely supported practice.

Appraiser Competence: One of the most dramatic consequences of regulatory oversight, and I include the HVCC in that category in spite of the fact that it was a forced policy, not regulation per se, is the fact that thousands of competent, experienced appraisers have been driven out of the industry due to the onerous requirements supported by HVCC and the Dodd

Frank Act. You will hear about this from today's witnesses. Not only has the competence of the appraiser community generally declined, with respect to geographic competence, since many of the AMC's are out of the state in which the property is, often the appraiser selected because they are willing to work for less and be subject to the rules of the AMC, is without the local expertise necessary to truly provide the value insights of a particular community.

<u>Appraiser Compensation and Consumer Cost:</u> Because of the practically mandatory use of a new middle man, the AMC, two things have happened in tandem, both negative. Appraisers whose fees have always been driven to competitive levels by the market have been reduced by requiring revenue for the AMC. At least a portion of this change has been borne by the consumer in the form of higher prices. In addition, when combined with the ineffective application of transportability, which was less frequently needed when local experts, the loan originators, ordered appraisals from local experts, the appraiser; many more redundant appraisals are necessary today leading to increased consumer cost and delayed closing or failed transactions.

<u>Inefficiency and Complexity:</u> The result of the myth-based reaction to a perceived, but unproven market issue, instead of achieving the stated goals of simplicity, clarity and accuracy the current regulated processes have led to market inefficiency and a level of complexity that frustrates sellers, buyers, lenders and leads to increased costs and failed transactions.

<u>Housing Recovery:</u> Possibly the most significant bottom line impact of the overzealous, misdirected and draconian intrusion in the market is the suppression on housing prices and recovery.

The committee will hear a variety of other insights from the witnesses, but **IMMAAG** believes that while there is value in regulatory guidance and it is difficult to escape an overreaction due to the depth of this century's financial crisis, this committee needs to send a message to the regulators that HVCC has been terminated and it is time to allow industry and the distribution system to return to the local, on the ground delivery mechanisms which were effective for decades and only failed when artificially overheated housing appreciation combined with a glut of unproductive, pent up capital led to excesses driven to convert locked up brick and mortar, paper net worth to spendable net worth.

There is no easy answer, but the chosen path has proven it is an obstacle to, not a solution for the problem the regulators feel they need to solve. Appraisal regulation has become the poster child for the wrong approach. Hopefully, our regulators and Congress can learn from that and reset the course by engaging industry in designing an effective solution.

In closing, I would like to make one final observation for the committee. Mortgages are delivered locally. Mortgage brokers (now called originators) were excluded from participating in the appraisal order process due to HVCC. Even in the face of congressional attempts to reverse that inappropriate reaction and even with the October 2010 termination of HVCC, the FHFA and the FHA have continued in their Appraiser Independence Requirements (A.I.R.) to refuse to change the processes. They continue to refuse to allow the most expert, most professional control source to be a participant in what is arguably the most empirically based tool a lender has to assess its understands its exposure in a purchase or refinance. In October 2010 I personally spoke with the attorney at the Federal Reserve Board who managed the Board's drafting and implementation of the Dodd Frank Act's required appraisal independence rule and was told by Ms. Kathleen Ryan that the Board did not intend the interim final rule to exclude mortgage brokers from the appraisal ordering or delivery process. I then spoke with management at both FHFA and FHA and was told that they did not care and intended to simply continue in the spirit of HVCC. A bad, questionably motivated local threat of litigation has become the foundation of the process that is central to managing housing finance risk and the regulators have done nothing to address. **IMMAAG** asks the Congress and this committee to take on that task and offers our expertise and the expertise of the thousands of state licensed mortgage loan originators who have not had a voice in this process to help.

Thank you for accepting **IMMAAG**'s comments. I look forward to the opportunity to assist.

William F. Kidwell, Jr. NMLS#174542