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# Appraisal Oversight: The Regulatory Impact on Consumers and Businesses

Testimony of Sara W. Stephens, MAI, CRE

Before the Subcommittee on Insurance, Housing and Community Opportunity

House Committee on Financial Services

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Madam Chairman Biggert, Ranking Member Gutierrez, and members of the Subcommittee on Housing and Community Opportunity, thank you for the opportunity to share our concerns regarding “Appraisal Oversight: The Regulatory Impact on Consumer and Businesses” on behalf of the more than 23,000 members of the Appraisal Institute, the largest professional association of real estate appraisers in the United States.

Today, residential appraisers face ever-mounting challenges that place the future of residential appraisal at risk. The appraisal regulatory structure has become almost entirely a “rules-based,” as opposed to a “principles-based,” system. As such, it has become a burden to appraisers and, in our view, has failed to improve overall appraisal quality or appraiser oversight and enforcement.

While appraising arguably is the most heavily regulated activity within the mortgage and real estate sectors, we warn Congress that a new and excessive regulatory regime is on the cusp of being enacted by appraiser regulatory agencies **without** Congressional review or authorization. This is a dangerous and unjustified move that risks hamstringing and jeopardizing the real estate appraisal profession altogether.

At a very basic level, the appraiser regulatory structure lacks fundamental accountability measures. In its report to Congress, the Government Accountability Office identified significant violations of internal control standards by entities that claimed such standards were designed to promote effectiveness and efficiency, and to promote accountability. We commend the GAO for these findings, yet, there are even more concerns that require further investigation and action by Congress.

Additionally, residential appraisers report that increased regulatory and investor requirements, coupled with client demands for cheaper and faster appraisals, have forced many highly qualified appraisers out of the mortgage appraisal business, or out of the profession altogether. Failures by bank regulators and financial institutions to enforce and adhere to basic appraiser independence requirements have turned the appraisal procurement system upside-down, revealing core, underlying weaknesses that place a drag on appraisal quality.

We believe that there is a better way forward – but it requires engagement and action by Congress. To date, Congress has chosen to review the appraisal regulatory structure only once in 20 years. This cannot continue, as the regulatory structure of today is nothing like what Congress enacted more than 20 years ago. Professional real estate appraisers throughout the country are united in calling on Congress to enact structural reforms that realign appraisal regulations to focus oversight and declining enforcement resources where they are needed most; to eliminate or curtail rules that hamstringing the appraisal process; and to support full consumer disclosure of fees relating to appraisal management processes.

## **Part 1. The Appraisal Regulatory Structure**

### *Appraisers Are Overwhelmed by Rules and Regulation*

Real estate appraisers apparently have the most complicated and convoluted regulatory structure of any profession in the United States. While certification and licensure are common for many industries, in 1989, Congress enacted a federal overlay that created a federal agency called the Appraisal Subcommittee (ASC), and then authorized a private organization, The Appraisal Foundation (TAF), to promulgate federally-funded standards and qualifications. For the past 20 years, every state has established an appraiser regulatory agency to conduct licensing and oversight activities. State appraiser licensing requirements must satisfy those imposed by the Appraiser Qualifications Board of TAF, and states also must enforce appraisers utilizing the Uniform Standards of Professional Appraisal Practice (USPAP), which is codified in every state and published by the Appraisal Standards Board of TAF. To complete nearly all residential mortgage appraisals, an appraiser must be certified or licensed in a state, and must adhere to USPAP. Failure to do so can lead to disciplinary action by state appraisal boards and/or criminal prosecution by law enforcement agencies. Often, a complaint or accusation alone submitted to a state appraisal board is sufficient for a client to remove an appraiser from their approved appraiser list.

On top of these requirements, the Government Sponsored Enterprises (GSEs), Federal Housing Administration (FHA) and other federal agencies maintain supplemental requirements that are imposed on lenders selling or

delivering loans to those agencies. For instance, Fannie Mae and Freddie Mac each have Seller/Service Guidelines that contain specific requirements for lenders relating to appraisals. As one example, the Seller/Service Guidelines require that comparable sales be no more than 12 months old. These requirements are often supplemented further by individual investor requirements that seek to comply with guidelines issued by the GSEs or FHA, or others in the secondary market. The imposition of several investor requirements has resulted in some lenders now requiring appraisers to include eight or nine comparable sales, where only three are required by the GSE seller/service guidelines. These requests for more information often are not found in the original scope of work, and appraisers therefore are not paid for the time and effort involved in conducting additional research. In recent years, appraisers have referred to this phenomenon as “scope creep,” and their frustration is heightened given that many of requirements to add comparable sales just to satisfy lender requirements provides little or marginal benefit to the assignment results.

Further, over the past year, Fannie Mae and Freddie Mac have embarked on the Uniform Appraisal Dataset (UAD), which attempts to mine data from appraisals and perform cursory reviews prior to funding decisions. The UAD was established, in part, because the GSE’s have admitted that their previous processes relating to appraisals failed. Fannie Mae or Freddie Mac only saw an appraisal if the loan went into foreclosure. While lenders are expected to conduct a thorough review of all appraisals prior to funding loans, that same expectation did not exist for the GSEs. The only information relating to the appraisal that the GSEs obtained prior to making a loan funding decision was the property’s address and its market value. In essence, Fannie Mae and Freddie Mac delegated all of the appraisal review functions to lenders who were selling loans to the GSEs, and who were making loan decisions without all of the information relating to the collateral offered. UAD attempts to address this by establishing a system of quick quality control review of appraisals prior to making funding decisions. Additionally, the system is being used to track the performance of appraisers, for example, checking to see if Quality or Condition Ratings of properties used in multiple appraisal reports are consistent.

Of course, the new UAD comes with a set of rules that appraisers must adhere to for the loan to be eligible for sale to Fannie Mae and Freddie Mac. Among other things, the UAD requires appraisers to select responses to predetermined and defined fields within the Uniform Residential Appraisal Report (URAR), a form also established and maintained by Fannie Mae and Freddie Mac that is now considered the industry standard for most residential appraisals delivered to lenders or to the secondary market. For example, the UAD established a new ratings system for property condition and quality. Properties are now rated by appraisers on a scale of 1-6 for both condition and quality. Elsewhere within the URAR, appraisers are asked to make selections from predetermined drop-down boxes, with all of this information being captured by the GSE’s for review of the information within the appraisal and performance measures of the appraisers.

#### Appraisal Practices Board

On top of all of the requirements established above, the regulatory burden for appraisers is on the cusp of being expanded exponentially because of a decision by TAF and the ASC to create something called an “Appraisal Practices Board” (APB). Congress restricted authorizations for TAF to the areas of appraisal standards and appraiser qualifications – Congress **did not** authorize TAF to codify appraisal methods and techniques. This new board’s supposed purpose is to establish what TAF claims are “voluntary guidelines” for appraisers and state regulatory agencies. Some state Agencies already may have assumed that they must incorporate the APB positions into law.

The APB concept is a major departure from the consensus between the Federal government and the appraisal profession in the late 1980s. The stakeholders and Congress agreed that Federally Related Transactions needed a mandatory set of standards to increase confidence in the valuation of properties for federally related lending. Leading organizations in the profession contributed their existing standards to form a basis for a mandatory standard to be known as The Uniform Standards of Professional Appraisal Practice (USPAP). The contributed standards still form the core of USPAP. The understanding at that time, between Congress and the stakeholders, was that TAF would maintain the mandatory standards but voluntary guidance and voluntary standards relating to methods and techniques, along with educational offerings related to the body of knowledge would remain in the domain of the profession and academia. This consensus worked for almost 20 years. Unfortunately promotion of the Appraisal Practices Board by ASC and TAF dangerously casts consensus aside.

In order to understand this issue fully, some explanation of the difference between appraisal standards and appraisal methods and techniques is required. Appraisal “standards” are guiding mandatory principles, and they are “standard,” meaning their application does not change much, if at all, with the situation. They involve broad, general concepts. Appraisal standards (i.e., USPAP in the United States) define such things as ethics and general steps needed for credible appraisal development and reporting. Conversely, “methods and techniques” are fluid. In other words, what they are and how they are applied is highly dependent on the specific circumstances. Those circumstances may be described as “best practices;” however, by its very definition, “best practices” are voluntary and cannot be codified.

Appraisal methods and techniques require *judgment* by the appraiser. It is assumed that the appraiser has been thoroughly trained to judge appropriate situations. The choice of methods and techniques are the responsibility of the appraiser in the development of his/her scope of work. Whether to use reproduction cost or replacement cost or when and how to adjust for sales concessions are dependent on the actions of the marketplace and should not be mandated by a body such as the APB. Real estate property types and markets are both extremely diverse. As a result, hard “rules of thumb” do not work within real estate appraisal because there always is an exception to the rule. What is more important is for the analysis conducted by the trained appraiser to be *thorough* and *credibly supported*.

Ever since the U.S. real estate appraisal profession was formally established some 80 years ago, appraisal methods and techniques have been limited to the academic community and professional appraisal organizations, not government agencies or those given certain authorizations by Congress. This was an important distinction established by Congress when it enacted the current appraisal regulatory structure in 1989.

#### Professional Appraiser Concerns

Even if the profession were to adopt a new trend of voluntary standards, TAF does not appear to have the capability to comply with cardinal rules of voluntary standard development. One need only examine the mission of longstanding Voluntary Standards Organizations such as the American National Standards Institute (ANSI), to note significant divergence.

From ANSI:

#### ***Q: How does ANSI conduct its business?***

***A: Overall, the Institute provides and promotes a process designed to protect the rights and interests of every participant through a set of four "cardinal principles."***

- *Openness – The ANSI process is fair and open. Any materially affected and interested party shall have the ability to participate.*
- *Balance – Participants should represent diverse interests and categories, and no single group should have dominance in standards development.*
- *Due Process – All objections shall have an attempt made towards their resolution. Interests who believe they have been treated unfairly have a right to appeal.*
- *Consensus – Agreements are reached when more than a majority, but not necessarily all, of the participants concur on a proposed solution.*

TAF and its APB are severely deficient in these areas.

In July 2011, the Appraisal Institute submitted testimony to this Committee outlining concerns regarding the decision to establish the APB, particularly the involvement of the ASC in its establishment and the virtually limitless authority of the new board. Over the past year, our concern about the negative impact of this board has only grown.

TAF, through its APB, is attempting to assert itself as the ultimate authority over all appraisal methods and techniques. This is problematic because the APB is not authorized by Congress, even though the average person would never know this because TAF consistently mentions it in the same breath as the “Authorized by Congress”

AQB and the ASB. We believe that Congress should exercise oversight over this insidious attempt to confuse the public by subtly abusing existing Congressional authority.

There are several reasons for our concern over the Appraisal Practices Board, as follows:

1. The establishment of the Appraisal Practices Board evidently was directed by the ASC or some of its influential members. When Congress established licensing and certification requirements for appraisers, it did not intend for the valuation process to be dictated by bank regulatory agencies, who, frankly, are not sufficiently staffed to delve into appraisal standards, let alone appraisal methodology. Here, it is worth noting that certification and licensing requirements apply to all types of federally related transactions, including residential and commercial real estate, so the impacts of this new entity truly impacts, and potentially creates a host of unintended consequences for, the entire profession.
2. The Appraisal Practices Board was established, despite strong objection from at least one federal bank examination agency representative on the TAF Task Force on Best Practices. According to a memo from a subject matter expert from the Federal Reserve of Atlanta that was sent prior to the release of the Final Report:

*“However, it is neither my recommendation to the Board staff as an assigned “technical resource,” nor the Board staff’s position that the Federal Reserve would be in favor of the creation of a separate ‘Best Practices’ Board. The structure of ASB and AQB being solely liaisons to this Board are also problematic and something I would advise against as a “technical resource.”<sup>1</sup>*

We understand that this position was agreed to by at least one other federal agency, in addition to the regional banks of the Federal Reserve. Further, it is worth noting that Federal funds were approved for reimbursement by the ASC to TAF for the purposes of this Task Force’s activities.

3. The APB was established under a false premise – that timely guidance materials on appraisal methods and techniques do not exist for appraisers. On the contrary, ample guidance and education materials are widely available to all appraisers in the United States. As just one example, the *Appraisal of Real Estate, 13<sup>th</sup> Edition* is cited in more than 700 court decisions in the United States. As another, the Appraisal Institute developed a residential seminar – “Appraisal Challenges: Declining Markets and Sales Concessions” – prior to the market crash in 2007, and delivered this seminar to thousands of appraisers throughout the country. Other cutting edge and timely seminars have been developed and made available to the entire profession on such issues as declining commercial real estate valuation and use of statistics and new technology within appraisal practice. While the Appraisal Institute has 23,000 members, our education is available to all appraisers. In fact, the vast majority of appraisers have taken education from the Appraisal Institute in recent years.
4. Codifying appraisal methods and techniques will curtail innovation within the industry, and stunt the development of new methods and techniques, essentially putting the profession at risk. If such requirements had been in place 50 years ago, the development and integration of discounted cash flow techniques within the income approach of appraisal would have been difficult, if not impossible to do, as only those methods that are *recognized* would be allowed by law. This decreases the ability of appraisers to integrate new technological developments and to respond to and develop solutions that address actual market conditions.
5. Codifying appraisal methods and techniques exponentially increases the regulatory burden on appraisers and their clients. Having to adhere to a USPAP that changes every two years is enough, let alone adhering to agency and investor requirements. However, having to follow guideline documents as long as 50 pages in length dramatically increases compliance costs on appraisers and consumers of appraisal services. Further, codification of methods and techniques places far too much emphasis over the *performance of methods and techniques* (following the letter of the law) than applying appraisal principles to given situations.
6. Codifying methods and techniques increases the unlevel playing field real estate appraisers have with other valuation professionals, including CPAs and others involved in business and personal property

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<sup>1</sup> Memo from K.C. Conway to David Wilkes regarding “Response to Draft Task Force Report to the Appraisal Foundation Board of Trustees,” August 17, 2009. Available at <http://www.appraisalinstitute.org/bg-pdfs/aug17-09-memo-aug21-best-practices.pdf>

valuation. The guidance documents under development by the Appraisal Practices Board are multi-disciplinary, meaning they may be developed for real estate appraisal, but also, for business and personal property appraisal. Unlike real estate appraisers, CPAs, business and personal property appraisers have no certification or licensing requirements, nor any governmentally enforceable standards. As a result, adding an additional layer of rules and regulations around appraisal methods and techniques serves to place real estate appraisers at a competitive disadvantage where these sectors compete. This includes advisory services, valuation for financial reporting, and the valuation of hotels and motels and special purpose properties, such as convenience stores and car washes.

7. If the APB "Valuation Advisories" to date are any example, at least from a real property perspective, they generally add nothing new to the appraisal body of knowledge. For the most part, APB Valuation Advisories 2 and 3 mostly quote the previously referenced *The Appraisal of Real Estate* and USPAP.
8. Attempting to codify appraisal methods and techniques "flies in the face" of judicial discretion and Supreme Court rulings. By proposing to codify specific methods and techniques within USPAP, TAF is proposing to limit the types of evidence courts and regulatory bodies may consider. This is contrary to a recent Supreme Court ruling which affirmed that courts have the ability to determine whether valuation methodologies are reliable in any given instance or case. Further, this decision correctly states that appraisal is an applied science, even a craft.<sup>2</sup> Further, there is no list of what makes expert testimony credible. Expert testimony exists to educate the court, and courts have the discretion to decide for themselves what credible support for their education is<sup>3</sup>.

#### Role of the ASC in the Creation of the APB

As we stated before this Committee last year, we have firm grounds to believe that the creation of the APB was inappropriately directed by the ASC, a move that is well beyond the statutory authority granted to the ASC by Congress.

Last year, this Committee received testimony from the ASC that it played no role in the establishment of the Appraisal Practices Board<sup>4</sup>. This statement contradicts the plain facts, which establish that the ASC was very much involved and participated in a highly orchestrated and concerted effort to create the Appraisal Practices Board. (A timeline of events may be found below.)

#### 2008

- In December 2008, the ASC held a board meeting where the issue was discussed and at least two members of the board of the ASC encouraged TAF to undertake efforts to address appraisal methods and techniques (effectively driving a wedge between TAF and the Appraisal Institute). The meeting minutes acknowledge that such a move would be viewed negatively by professional appraisal organizations, so TAF successfully sought the support of the ASC in pursuit of the endeavor, stating:

*V. Gibbs and S. Gardner discussed their desire to have the USPAP include more direction on appraisal methodology. D. Bunton expressed a concern that encroaching on areas like methodology and instruction could potentially be viewed as "mission creep," particularly by Appraisal Foundation sponsoring organizations. S. Gardner stressed the need to venture into these areas to improve on concerns the ASC member organizations are seeing in the appraisals*

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<sup>2</sup> See *CSX Transportation, Inc. v. State Board of Equalization of the State of Georgia*. "Valuation is not a matter of mathematics, as if the district court could prevent discriminatory taxation simply by double checking the State's assessment equations. Rather, the calculation of true market value is an applied science, even a craft. Most appraisers estimate market value by employing not one methodology but a combination. These various methods generate a range of possible market values which the appraiser uses to derive what he considers to be an accurate estimate of market value, based on careful scrutiny of all the data available." Available at <http://www.appraisalinstitute.org/bg-pdfs/CSX.pdf>

<sup>3</sup> See *Daubert v. Merrell Dow Pharmaceuticals*, a rule of evidence regarding the admissibility of expert witness testimony.

<sup>4</sup> At the July, 2011 hearing, Chairman Biggert asked what role, if any, the Appraisal Subcommittee played in the establishment of the Appraisal Practices Board. Mr. Park stated: "The Appraisal Subcommittee played no role in the creation of the practices board."

provided to their member banks and institutions. S. Guilfoil requested assurance that the ASC would support ASB efforts in this regard. S. Gardner provided the assurance and indicated the ASC would issue a letter, if necessary, with its specific request for this change in USPAP<sup>5</sup>.

## 2009

- On January 21, 2009, TAF sent an email explaining that the ASC “expressed a strong concern” to TAF that timely guidance to appraisers does not exist. This email also advised that members of the ASC would help comprise a task force to explore the issue<sup>6</sup>.
- On January 27, 2009, the TAF President sent an email explaining the make-up of the task force, stating, “Since the genesis of this issue came from the ASC, they will be appointing two representatives.”<sup>7</sup>
- On February 9, 2009, TAF sent a letter warning the Appraisal Institute that inquiries regarding the ASC concerns were a “private matter” involving TAF and the ASC<sup>8</sup>.
- In April 2009, TAF advanced an amendment before this Committee for TAF to codify “best practices” and to be the authority for appraisal methods and techniques. The ASC participated in meetings with TAF as it sought the support of AI for the amendment. Ultimately, this amendment was not offered during the Dodd-Frank deliberations and was not considered by the Committee<sup>9</sup>.
- In late April or early May 2009, two ASC board members were removed from the task force and replaced by two individuals, one from the Federal Reserve Bank of Atlanta and the other from a regional field office of the Office of Thrift Supervision, reportedly, because of legal and conflict of interest concerns.
- In the summer of 2009, the Federal Reserve Bank of Atlanta official participated in a phone conversation with the executive director of the ASC and the ASC board member from the Federal Reserve to discuss the task force and appraisal methods and techniques. The parties discussed funding options for development of “best practices” and TAF involvement in the development and delivery of education, including coordination for how TAF would issue Requests for Proposals.
- On August 17, 2009, the new task force representative from the Federal Reserve Bank of Atlanta expressed concerns in writing over the recommendations of the task force.
- In September 2009, the task force released its recommendations, which called for a panel to be established by TAF to develop recognized methods and techniques. In September 2009, the ASC approved a funding reimbursement request for activities related to the task force that led to the Appraisal Practices Board. In addition, the TAF chairman of the board presented to the ASC a grant funding request to fund methods and techniques activities for \$275,000 in 2010. According to the Public Meeting Minutes, “D. Bunton said that the grant request should be finalized by the Foundation Board of Trustees in November and available for approval by the ASC meeting in December. He said that the Foundation is estimating the grant request will be in the area of \$2.3 million. This is an increase of approximately \$335,000 over the 2009 grant. Approximately \$275,000 of this increase will be for the Recognized Methods and Techniques Panel (RMAT) on real property valuation.”<sup>10</sup>
- In October 2009, TAF Board of Trustees approved the establishment of a third board – the Appraisal Practices Board – ignoring the task force’s recommendation to establish a Recognized Methods and Techniques panel<sup>11</sup>. According to the Task Force’s report, “At this time, and for purposes of

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<sup>5</sup> From the ASC Meeting Minutes, December 2008,

<https://www.asc.gov/Documents/MeetingMinutes/ASC%20Bd%20Mtg%20Minutes%2012.11.2008.pdf>

<sup>6</sup> From the ASC Meeting Minutes, December 2008,

<https://www.asc.gov/Documents/MeetingMinutes/ASC%20Bd%20Mtg%20Minutes%2012.11.2008.pdf>

<sup>7</sup> From Email from David Bunton. Available at <http://www.appraisalinstitute.org/bg-pdfs/GenesisASC.pdf>

<sup>8</sup> Letter from Appraisal Foundation to Appraisal Institute, February 9, 2009. Available at

<http://www.appraisalinstitute.org/bg-pdfs/privatematter.pdf>

<sup>9</sup> From Appraisal Foundation Letter to the Subcommittee on Capital Markets. April 22, 2009. Available at

<http://www.appraisalinstitute.org/newsadvocacy/downloads/TAFbestpracticesproposal.pdf>

<sup>10</sup> From the Task Force Report to the Board of Trustees, September 11, 2009, available at

[http://www.appraisalinstitute.org/newsadvocacy/downloads/TaskForceMemo\\_BOT\\_091109.pdf](http://www.appraisalinstitute.org/newsadvocacy/downloads/TaskForceMemo_BOT_091109.pdf)

<sup>11</sup> Memo from Paul Welcome, Chair of TAF Board of Trustees to Sponsoring Organizations, October 26, 2009.

Available at <http://www.appraisalinstitute.org/bg-pdfs/diversion.pdf>

*expediency, we suggest that the RMAT be constituted in the form of a panel; with time and proper funding, the panel may develop into or report to a third "board" under BOT oversight (similar to AQB and ASB) that oversees recommended methods and techniques in various appraisal disciplines."*

- Further, leaders of the Appraisal Institute were informed directly by the TAF President that TAF was "told to do it" by the ASC. Appraisal Institute leadership will provide affidavits to these comments, if deemed to be helpful.
- On September 15, 2010, the 2010 TAF Chairman conducted a media interview where he stated to "The Housing Helix" podcast, "The Appraisal Practices Board is a good example...we were asked by the ASC to do this, not informally, but its members expressed an interest in the Foundation doing this at least."

In November 2009, TAF officially commenced the Appraisal Practices Board with a solicitation for members of this board. In July 2010, the Appraisal Practices Board began its operations and, on December 22, 2011, released its first exposure draft. In May 2011, the ASC reported to this Committee that TAF had established the Appraisal Practices Board.

#### Appraisal Subcommittee Authority

Any directive by the ASC and its members to establish a new board – without Congressional authorization – goes beyond the ASC's legal mandate to monitor and review activities of TAF related to standards and qualifications as authorized under Title XI. The ASC does not have the authority to direct TAF to take certain actions. Specifically, according to correspondence from the Appraisal Subcommittee, *"Although Title XI does mandate that the ASC 'monitor and review the practices, procedures, activities, and organizational structure of the Appraisal Foundation' and the AQB, Congress did not provide the ASC with the authority or the power to direct or overrule the operations or structure of these private entities."*<sup>12</sup> Our organization is not aware of the ASC advising Congress of any concerns regarding areas of appraisal practice and recognized methods and techniques, as well as any perceived disconnect between appraisal standards and appraisal practice. Expression of such concerns in the ASC's Annual Report or in other forms of correspondence would have been an appropriate conveyance of the ASC's monitoring and review authorization; yet none can be found in any public Report to Congress<sup>13</sup>.

Regardless of whether the ASC directed or only expressed interest in the establishment of the Appraisal Practices Board, we believe Congress should be concerned that such orchestration would continue to occur without any authorization in this area. In our view, this orchestrated event is enabled by a regulatory structure that lacks appropriate Congressional oversight and accountability.

#### GAO Findings and Recommendations

In January 2012, the Government Accountability Office (GAO) released a report citing the need for the ASC to establish policies and procedures related to TAF funding eligibility. Specifically, the GAO report cited the ASC for not having specific policies for determining whether activities of TAF (a private nonprofit organization that sets criteria for appraisals and appraisers) that are funded by ASC grants are Title XI-related. Not having appropriate policies and procedures is inconsistent with federal internal control standards designed to promote effectiveness and efficiency and 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 ASC and TAF has insufficient accountability measures. Outside of preparing an annual report to Congress, oversight of the ASC is virtually non-existent. We note that the agency does not have an inspector general who can conduct independent assessments of the ASC's programs and operations.

Further, it is interesting to note that one day after the public release of the GAO report, the former chair of the ASC was replaced. Although no explanation has been given to date, the timing of these replacements implies a direct relationship with the public release of the GAO report.

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<sup>12</sup> From Appraisal Subcommittee correspondence with George R. Harrison, Ph.D., September 11, 2002, available at <https://www.asc.gov/documents/othercorrespondence/ltr%20harrison%20request%2009.11.02.pdf>

<sup>13</sup> ASC Annual Reports are available at <https://www.asc.gov/About-the-ASC/AnnualReports.aspx>

In essence, the ASC reshuffled its board, but the basic lack of fundamental oversight and accountability measures remains. By the actions described above, the relationship between the ASC and TAF has become far too cozy and perhaps even a bit incestuous. As an example, a former TAF employee – who worked directly for the TAF president – was hired as the ASC executive director and is now charged with overseeing/monitoring its operations, including its relationship with TAF.

#### Original Plan of the ASC/TAF Advances Without Congressional Authorization

Even though Congress did not authorize TAF to be the source for appraisal methods and techniques, or “best practices,” during the Dodd-Frank deliberations, this has not impeded that plan from being executed. Over the past six months, the Appraisal Practices Board has begun publishing “valuation advisories,” which claim to produce “voluntary guidance” for appraisers on such issues as what types of comparable sales are used or how to adjust for sales concessions in the market.

During the exposure draft period for the valuation advisories, we requested that the Appraisal Practices Board clarify and confirm that the advisories are **purely voluntary** in scope and cannot be used for discipline or enforcement purposes. To date, this request has been plainly ignored or denied. In addition to TAF’s proposal to Congress to codify “best practices,” the basis for this concern is that the Appraisal Practices Board is speaking inconsistently. On the one hand, TAF claims the documents are voluntary; while on the other, they invite their codification. Specifically, the valuation advisory documents state: *Compliance with such guidance is voluntary, unless mandated through applicable law, regulation, or policy.*

Meanwhile, TAF representatives now are encouraging states to make valuation advisories from the Appraisal Practices Board compulsory. At the April 2012 meeting of the Appraisal Qualifications Board, representatives from TAF encouraged state appraiser regulatory agencies to use the valuation advisories when bringing enforcement actions against appraisers. Additionally, appraisers were warned at the April 2012 meeting of the Association of Appraiser Regulatory Officials (AARO) that veering from the valuation advisories could result in a disciplinary action.

Further, the Appraisal Standards Board of TAF released a proposal on May 24, 2012, that effectively would codify the works of the Appraisal Practices Board within USPAP itself. Specifically, the Appraisal Standards Board has proposed to define appraisal methods and techniques within the USPAP Scope of Work Rule, citing the Appraisal Practice Board directly. USPAP has been published for more than 20 years without any specific reference to appraisal methods and techniques. Is it simply a coincidence that the first time this is advanced is immediately following the first release of valuation advisories from the Appraisal Practices Board? Comparatively, the *Appraisal of Real Estate, 13<sup>th</sup> Edition*, the most widely published text in the world illustrating appraisal methods and techniques, has never been referred to within USPAP, despite strong recognition throughout the judicial system.

The USPAP proposal raises serious concerns and questions about the independence of the Appraisal Standards Board which, according to TAF’s bylaws, is not to take any direction from the TAF Board of Trustees<sup>14</sup>. This proposal shows that the Appraisal Standards Board now may be doing the bidding of the TAF Board of Trustees to assert control over the entire appraisal process.

This is not the first time that we have seen or heard such a concern regarding the independence of the Appraisal Standards Board. Specifically, several former members of the Appraisal Standards Board (ASB) privately have expressed concern that the independence of the ASB may have been compromised by TAF’s Board of Trustees in recent years. According to TAF By-Laws, the ASB is to operate independently from TAF’s Board of Trustees with regard to the terms and content of USPAP.<sup>15</sup> Former members of the ASB report that members of TAF’s Board of Trustees directly interfered with the ASB’s duties and obligations, directing it to take certain actions or avoid taking others. We believe it is worth noting that members of the Board of Trustees and executive-level staff

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<sup>14</sup> “Except as otherwise provided in these Bylaws or by resolution of the Board of Trustees, the Standards Board shall have and exercise all authority and power and perform all functions of the Foundation and the Board of Trustees in respect to establishing improving and promulgating the terms and content of the Uniform Standards of Professional Appraisal Practice.” Available at <http://www.appraisal institute.org/bg-pdfs/tafbylaws.pdf>

<sup>15</sup> *Ibid*

of TAF and the ASC attend meetings of the Appraisal Standards Board that are closed to the public. Regarding this practice, as well as the situation involving the Task Force on Best Practices, we encourage Congress to speak with former members of the ASB to determine whether any actions by the ASC or TAF's Board of Trustees may have jeopardized or compromised the independence of the ASB.

#### Potential Explanations for the APB

There are several potential explanations for the establishment of the Appraisal Practices Board, as follows:

1. Federal funding. An original intent behind establishing the Appraisal Practices Board appeared to have been to position TAF to receive additional federal funding from the ASC, as a funding request immediately was made of the ASC by TAF. TAF revenues have declined substantially in recent years, so new funding streams had been sought by TAF to help offset recent losses. TAF leadership openly expressed its desire to seek federal funding for the APB, having advanced a legislative amendment to this effect that sought specific funding from the ASC in September 2009. TAF leadership also stated publicly that federal funding of the APB could follow a course similar to that of the ASB and AQB, which were created prior to Congressional authorization in Title XI<sup>16</sup>.
2. Education Development. Ultimately, it has been AI's long-held view that TAF's main goal was to enter into direct competition with private organizations in offering appraisal education. When TAF was formed in the 1980s, it was done with the understanding that it would not offer education, delegating that responsibility to professional appraisal organizations and academia. Contrary to any assertions made by TAF and the ASC, this process has worked well, as professional appraisal organizations have delivered timely education and guidance to the market. For example, courses relating to valuation in declining markets, sales concessions, and the valuation of "green" and/or energy-efficient features in properties were developed by the Appraisal Institute to fully prepare appraisers for emerging issues<sup>17</sup>. TAF's current policies appropriately limit TAF's development or delivery of education to appraisers on methodological issues. However, these policies are on the cusp of being dramatically revised. This follows a previous move into the USPAP education arena, a step taken by TAF approximately 10 years ago. At that time, TAF embarked on an initiative to develop education relating to USPAP. It was explained that this course was developed as a "benchmark" to which TAF could compare other organizations' courses for consistency with USPAP. Yet TAF does not require such "comparison" for any other courses developed by other organizations.

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<sup>16</sup> Presentation by David Bunton, President of TAF before the Association of Appraiser Regulatory Officials, May 1, 2010.

<sup>17</sup> We believe that Congress should be aware of a recent Memorandum of Understanding (MOU) between TAF and the Department of Energy (DOE) regarding "green" appraisal issues. This MOU helps to illustrate concerns regarding TAF's involvement in appraisal education and practice issues, while being the exclusive standards-setting organization for the appraisal profession. Among other things, the MOU outlines how DOE plans to develop an education course curriculum for appraisers based on works of the APB. A recent article from *Valuation Review* highlights what is planned with the APB:

*The Department of Energy wants to develop educational course curriculum for appraisers in valuating energy performance and sustainability in buildings. The appraiser practices board issues guidance in that area, which it would use as the basis for the course and then send it through the AQB course-approval program. The program would likely be an extra certification, in the way of continuing education offered by the Appraisal Qualifications Board (AQB). The board has added green buildings as one of its continuing education topics, and it may include green building valuation as a part of the primary qualifications criteria down the line, according to Bunton. After all that, it's not hard to imagine lenders engaging appraisers who have completed the Department of Energy curriculum.*

It is important to note that professional appraisal organizations already have responded with green appraisal education and credentialing programs. For instance, the Appraisal Institute has invested considerable resources to develop a three-part series, professional development program that specifically focuses on high performance (green) building valuation. The program provides appraisers with various methods and techniques that then can be utilized to analyze energy-efficient features in buildings.

Procedurally, TAF, despite numerous public denials, currently develops online USPAP education in concert with a private education provider, issuing a request for proposals and then licensing the education through this entity. While other organizations are welcome to develop their own USPAP courses, if they can afford it, such USPAP courses are judged in comparison to TAF's "benchmark," often resulting in cost-prohibitive changes. Thus, if the cost of trying to develop such proprietary courses is not cost-effective, TAF will "license" its benchmark course to that organization, provided that TAF receives compensation for each individual use. Please note that all appraisers *must* take a USPAP update course at least every two years.

Of greater concern is that TAF also is on the cusp of expanding its education to *all* areas of appraisal, including appraisal methods and techniques. It is apparent that TAF intends to pursue a path similar to what it did in entering USPAP education with regard to appraisal methods and techniques. Specifically, TAF recently formed another task force to help it develop a strategic plan. This task force, according to a verbal report delivered by the TAF President earlier this month, has recommended that TAF "develop education for appraisers."

This development is not surprising, given that one apparent motive to create an Appraisal Practices Board is to develop a "body of knowledge" of its own, even though one already exists within academia and the private sector. Twenty years ago, TAF did not develop guidance related to appraisal methods and techniques beyond any advice of the Appraisal Standards Board, nor did it offer education. It now does both, competing directly with private professional organizations that do not have the advantage of a Congressional imprimatur. TAF has done so while confusing and abusing authorizations from Congress, claiming implied consent from Congress that TAF is the source for appraisal methods and techniques. Such abusive behavior confuses the public and stands to further harm the appraisal profession.

We believe that Congress must establish limitations or parameters regarding TAF's work outside of its standards and qualifications responsibilities. Limitations relating to the APB should ensure that the appraisal profession is not handcuffed by procedural rules. Appraisers do not need more rules, but rather a return to fundamental principles that support market expertise and sound judgment. Conversely, if appraisers are going to have more rules to follow, clarity is needed for the roles of the parties involved in establishing those rules, how those rules are to be developed, and what limitations need to be imposed for TAF's involvement in other areas of professional activity and practice. As a private organization, we do not have the privilege or benefit of a "stamp of approval" from Congress, and yet we are faced with the proposition of having to compete in the area of education with such an entity. This is grossly unfair and not contemplated, nor authorized, by Congress.

#### Enhancing Oversight and Enforcement

One of the purported intentions for the establishment of the Appraisal Practices Board was to assist state regulators with conducting oversight and enforcement. According to the Final Report of the Task Force that led to the creation of the Appraisal Practices Board, "We also believe that this name will encourage appraiser regulatory agencies to reference the work product of this group."<sup>18</sup> However, even here, we believe that relying on the Appraisal Practices Board to conduct enforcement is misguided, and ignores more significant issues that impede enforcement processes by states.

In fact, while the APB has only begun to publish guidance materials, we already have identified at least one error that would result in inappropriate disciplinary action against appraisers. Further, should appraisers treat the document as if it were *compulsory*, it actually would lead to a rash of inaccurate appraisals<sup>19</sup>.

<sup>18</sup> From the Task Force Report to the Board of Trustees, September 11, 2009, available at [http://www.appraisalinstitute.org/newsadvocacy/downloads/TaskForceMemo\\_BOT\\_091109.pdf](http://www.appraisalinstitute.org/newsadvocacy/downloads/TaskForceMemo_BOT_091109.pdf)

<sup>19</sup> Specifically, the valuation advisory, "*Adjusting Comparable Sales for Seller Concessions*," explains that if sales concessions are paid by the seller in *virtually all sales transactions* (bold for emphasis), an adjustment may not be necessary since it would be typical of the market. This is referenced on pages 9, 10, 13 and 14 within the document. The purpose of adjusting comparable sales for concessions is to provide an indication of value of the subject property based on the definition of value. Even though the sales concession might be "typical" of the market and paid by the seller in virtually all transactions, the sale price is impacted by the concession. Furthermore, if the concessions are related to financing, the properties purchased with cash are atypical of the market and must be adjusted accordingly. Failing to adjust for sales or financing concessions, even though (cont).

In reality, the biggest challenge facing state appraiser regulatory officials is the lack of financial resources to hire qualified investigators to review complaints against appraisers and assist with prosecution. Often today, investigators share time with other licensing boards, ranging from barbers and beauticians to home inspectors and morticians. This places limitations on investigations involving appraisers, diluting the effectiveness of the state appraiser regulatory agencies in conducting oversight and enforcement.

One way to address this is to ensure that appraiser licensing fees are used by state appraiser regulatory agencies for appraiser oversight and enforcement through dedicated funds. Often, appraiser licensing fees are swept by state governors to help fill budget shortfalls or support non-appraiser oversight functions. Over the past year, the Appraisal Institute led an effort in the state of Maryland to dedicate appraiser licensing fees to appraiser oversight and enforcement. We have established model legislation for other states – approximately 15 – that are at risk of having funds swept for other uses.

Beyond state budgeting complexities, under the current structure, state appraisal boards send \$40 for every licensed appraiser to the ASC, which uses this money to fund its operations and grants to TAF. The Dodd-Frank Act authorized the ASC to provide grants to state appraiser regulatory agencies for enforcement purposes, however, no details for that program have been released. It would appear to us that appraiser licensing fees would be better spent directly by state appraiser regulatory agencies to hire qualified investigators and review appraisers to enforce and regulate.

Other challenges for oversight and enforcement include ensuring that those who oversee state regulatory boards, particularly their enforcement staff members, have the necessary appraisal education and/or familiarity with the appraisal body of knowledge. In some cases, members of these staffs do not have the qualifications to review appraisals submitted for enforcement. Those who oversee state regulatory agencies (“Policy Managers” at the ASC) should have the ability to determine not only the adequacy of enforcement in terms of expedition, but also the quality of the work being reviewed and the reviews themselves. While this may or may not require state licensure or certification, it should include the necessary education to achieve a license.

Also, both the standards-setting entity (i.e., ASB) and the oversight and enforcement agency need to monitor state regulatory boards so that enforcement over appraisers is consistently applied in every state/territory where USPAP is in effect. There is more than sufficient anecdotal evidence that different regulatory boards enforce USPAP in different ways.

We believe that Congress must establish laws that empower state appraisal boards to do thorough and fair investigations and to prosecute meaningful complaints involving appraisers. However, too often, it appears that the state appraisal regulatory agencies simply are attempting to clear a backlog of complaints to pass inspection by the ASC. State regulators appear to focus more on ministerial violations than on harder-to-prove ethics and competency violations. Here, we believe codifying the works of the Appraisal Practices Board compounds these problems, as it is likely that state appraisal boards will turn to these documents to demonstrate compliance to the ASC. Again, so-called voluntary guidance materials are at risk of being misused by enforcement agencies to the detriment of the appraisal profession and the public.

This challenge is not unique to real estate appraiser regulatory agencies, as appraisers are in fact well beyond most in the real estate and mortgage sector in actually establishing and maintaining an enforcement regime. However, other industries have established more efficient systems that share resources amongst agencies and focus financial resources where they are needed most. One such system is the National Mortgage Licensing System established by the Conference of State Bank Supervisors. This system is a cooperative amongst state licensing agencies for mortgage brokers and mortgage loan officers. Now recognized by Congress, the system enables mortgage originators to fill out a single application and to apply for licensure in multiple states. On the enforcement side, the NMLS allows state agencies to share information and track individuals moving or doing

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seller-paid concessions might be prevalent in the market, is not proper guidance when the definition of value includes a price unaffected by sales or financing concessions. Further, it is a strong example for why voluntary guidance materials should never be used as compulsory documents.

business across state lines. And it does this without convoluted federal layers that drain precious resources that could be used for state oversight and enforcement.

## **Part 2. Appraisal Independence and Procurement**

We often hear from real estate agents, home builders and others that appraisals are “killing deals,” and/or holding back the economic recovery. These accusations are unfounded and misguided, as appraisers do not “make the market,” but rather “reflect or report the market.” To this point, appraisals are an important risk management activity to be conducted by banks in making safe and sound lending decisions. Appraisals are not meant to simply support contracts – they are obtained to help lenders assess their overall risk. Fundamentally, it does neither the borrower nor lender any good to enter into a mortgage for more than the value of the property.

Still, there is a significant inconsistency found in Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989. FIRREA requires certification or licensure for appraisers, but it also prohibits banks from establishing appraiser hiring policies that recognize credentials beyond the minimum requirements. In a time when home builders and others are requesting the use of professionally designated appraisers, lenders are actually prohibited by law from seeking out the most qualified appraisers. One purpose behind this provision was to help establish certification and licensure by states. At the time of enactment, some were concerned that allowing lenders to require certain professional designations would impede development of a pool of appraisers. This provision has long out-lived its useful purpose, and we believe it should be reconsidered in an effort to promote higher quality appraisals.

Beyond this, to the extent that there is a crisis of confidence regarding appraisals, this is a direct result of the way in which lenders, under the oversight of bank regulatory agencies, procure appraisals today. Here, the predominant factors in the appraiser hiring decision often are price and turnaround time of the appraisal, not quality of service, or geographic or market competency of the appraiser. Mortgage lenders have it within their ability to address these concerns, and we urge them to do so immediately.

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

1. Federal regulatory agencies are deeply understaffed to deal with examination issues involving appraisals. At one point in the 1990s, each federal regulatory agency had competent appraisers on staff helping to support examination teams. Today, there are a total of two professional designated real estate appraisers supporting examination functions in all four of the major examination agencies. While the OCC recently published an appraisal support position at headquarters, the response of other bank regulatory agencies is woefully deficient and must be enhanced to deal with the various collateral valuation challenges facing regulators and financial institutions today.
2. Federal bank examiners have identified widespread problems with the way in which many banks have handled appraisal administrative duties. A recent review by the Appraisal Institute of Material Loss Reports indicates that 75 percent of now-failed banks had been previously cited for various appraisal violations, often failing to obtain appraisals where required, or having insufficient resources within the bank to manage and oversee the appraisal function.
3. Generally, most banks have failed to take responsibility or ownership of the appraisal function, electing to outsource appraisal operations to mortgage brokers, who have a vested interest in the transaction, or to third party appraisal management companies, that offer a layer of insulation from coercive pressure, but apply new business pressures that put constraints on appraisal quality. This is evidenced by a slew of lawsuits, settlements and other regulatory actions that cite widespread deficiencies regarding appraisal independence and appraisal quality, including the Ameriquest settlement with 48 state attorneys general; the Home Valuation Code of Conduct, resulting from a settlement agreement with the New York Attorney General's office; various lawsuits from the Federal Housing Finance Agency and Federal Deposit Insurance Corporation; and out of court settlements with “whistleblowers” who attempted to report apparent violations of appraisal rules within banks, but faced threats and retaliation from their employers.

As a result of these and other issues, the natural reaction of many banks and financial institutions has been to establish a hard firewall between loan production and risk management functions and appraisal. Such a firewall inhibits communication between the underwriting staff and the appraiser to the point that causes more damage to the process than it helps. Many are under the mistaken impression that federal rules now require the use of appraisal management companies (AMCs) to comply with basic appraisal independence requirements. This is not the case, as banks can manage the appraisal ordering and review internally. Many banks, 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 can 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 a best practice that more banks should follow. Too few resources have been devoted to appraisal staff within financial institutions, as evidenced by Material Loss Reports, which often cite banks for failure to devote staff to obtaining credible appraisals. Moving forward, we believe that incentives, such as higher marks on CAMELS ratings, should be established for banks to maintain rigorous risk management positions in support of collateral risk management.

This is not to say that *all* AMCs 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 significant failures. Our biggest concern is the propensity to make appraiser hiring decisions 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 factor in the appraiser hiring decision. Yet, as cited above, bank regulatory agencies appear understaffed to enforce this provision, helping to enable substandard appraisal procurement by banks.

The viability of the predominant business utilized by appraisal management companies may not be sustainable. In fact, several large appraisal management companies have failed recently, stiffing appraisers for millions of dollars in appraisal fees. Last month, a Phoenix judge concluded that a large AMC failed to pay appraisers in Arizona at least 171 times within the past 18 months. The judge recommended that the Arizona Board of Appraisal fine the company \$850,000 and revoke the company's registration as an appraisal management company.

One positive from this situation was that a major client of the failed appraisal management company (Appraiser Loft) made good on the appraisal fees that were owed to appraisers, paying appraisers who had unpaid invoices. Commendably, the chief appraiser of this bank (MetLife) was quoted in a media report as follows:

*It's not the appraiser's fault that AppraiserLoft didn't pay them. If an appraiser did the work and we made a decision based on the appraisal provided - the appraiser should be paid<sup>20</sup>.*

Unfortunately, it's more common that these bills go unpaid when an appraisal management company fails. One infamous case involves Taylor Bean Whitaker (TBW), who once was one of the largest wholesale lenders in the country, but ceased its operations after a raid by the Federal Bureau of Investigation and a suspension by the FHA. TBW owned an appraisal management company – Security One Valuation Services – which left numerous appraisers with unpaid invoices. This trend does not appear to be ceasing, as evidenced by a letter that we received from a member earlier this week.<sup>21</sup>

It should be noted that many banks are using the AMC as profit centers at the expense of the appraiser. Some of the largest AMCs are owned by banks. Prior to the recent advent of AMCs, banks either reviewed all appraisals by staff or outside contract. Now, the banks establish an AMC, order and review all appraisal through the AMC, and reduce the fee to the appraiser while keeping the AMC fee (typically as much as half of what they pay appraisers) for themselves.

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<sup>20</sup> From Appraiser Talkback Blog, March 15, 2012, available at <http://www.orep.org/wordpress-2.7/wordpress/?p=521>

<sup>21</sup> Letter to Sara Stephens from Stephen P. Kurilchyk, SRA, June 20, 2012. Available at <http://www.appraisalinstitute.org/bg-pdfs/kurilchyk-sra-letter.pdf>

### Interim Final Rule & Customary and Reasonable Fees

The Dodd-Frank Act contains a provision requiring “customary and reasonable” fees be paid to appraisers to reflect what an appraiser would typically earn for an assignment absent the involvement of an appraisal management company (AMC). 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. This issue is extremely important given evidence that indicates wide divergence between fees paid to appraisers through appraisal management companies and those retained directly by financial institutions. While some AMCs pay full fees and charge for their services on a “cost-plus” basis, many do not.

This provision required the Federal Reserve to develop a rule within a very short time period. The Federal Reserve published an Interim Final Rule for comment, but took no action there further. As a result, the Interim Final Rule became effective on April 1, 2011. We do not believe the Interim Final Rule is consistent with the plain language and intent of the Dodd-Frank Act.

Under the Interim Final Rule amending Regulation Z (Truth in Lending), lenders and their agents are provided with two presumptions of compliance. The first option states that lenders will be presumed to comply if the amount of compensation is reasonably related with recent rates (last 12 months) for appraisal services performed in the geographic market of the property. The creditor or its agent must identify recent rates and make any adjustments necessary to account for specific factors, such as the type of property, the scope of work, and the fee appraiser's qualifications; and the creditor and its agent do not engage in any anticompetitive actions in violation of state or federal law that affect the rate of compensation paid to fee appraisers, such as price-fixing or restricting others from entering the market. The Fed's commentary on the first presumption states that AMC fees are an acceptable component of the factors used by creditors and their agents to establish compliance with the statute's customary and reasonable mandate. As stated above, our organizations strongly object to this feature of the IFR and have urged its removal.

Under the second presumption of compliance, a lender or agent is presumed to comply if it establishes a fee by relying on rates in the geographic market of the property being appraised or established by objective third-party information, including fee schedules, studies and surveys prepared by independent third parties such as government agencies, academic institutions and private research firms. The interim final rule follows the statute in requiring that fee schedules, studies and surveys, or information derived from them, used to qualify for this presumption of compliance must exclude compensation paid to fee appraisers for appraisals ordered by appraisal management companies.

We believe that the two presumptions of compliance are inconsistent with one another. While the second presumption specifically excludes assignments ordered by known appraisal management companies, the first presumption specifically does not require that a creditor use third-party information that excludes appraisals ordered by AMCs. While this statement could be read to clarify the previous comment found in that paragraph that stipulates use of a fee survey or study is not required, a literal interpretation of this statement would create a significant departure from the intent of the legislation defining customary and reasonable fees as appraisal assignments absent the involvement of AMCs.

As such, we are not surprised to hear that the first presumption of compliance has been initially interpreted by some large banks and AMCs to mean the current business model employed by many banks and AMCs today is thought to be satisfactory. Unfortunately, all available evidence suggests this arrangement is totally inconsistent with the second presumption of compliance, as explained below.

The Interim Final Rule is inconsistent, ineffective and contrary to the spirit of the Dodd-Frank Act. The very existence of the customary and reasonable fee provisions of Dodd-Frank, together with the mandated exclusion of AMC fees in calculating what's customary and reasonable, results from Congressional recognition of the influences of AMCs on fee appraisers and their harmful impact on appraiser independence and the integrity of valuations in our mortgage lending markets.

### Consumer Disclosure Form/HUD-1

These problems are masked by consumer disclosure rules that currently allow co-mingling of appraisal and appraisal management company fees on the Appraisal line of the HUD-1 Settlement statement. Recent consumer research indicates that consumers are paying higher costs for appraisal fees as reported on the Appraisal line of the HUD-1 statement<sup>22</sup>. This co-mingling mistakenly confuses consumers into believing that they are paying appraisers more for services today, when in fact, compensation has declined as much as 40 percent.

As you know, the Dodd-Frank Act authorized separation of appraisal and appraisal management fees. We support this provision and believe separate disclosure should be required to fully inform borrowers of actual costs paid with regard to the appraisal process. This includes both the performance of the appraisal and any administrative and review functions. We see no consumer benefit with continuing to bundle two separate services, as is current practice today.

Traditionally, appraisal management fees were allocated as part of *loan processing or administration* fees or through the interest rate. However this has changed over the years as more lenders have outsourced appraisal functions to third party management companies. This is enabled by interpretations of the Real Estate Settlement Procedures Act, the foundation of which dates back to the origins of the HUD-1 in 1974, long before the current appraisal management business model was established. This allows the bundling of appraisal and appraisal management expenses when appraisal management companies are used. A change here is long overdue.

However, the CFPB, through the establishment of a new Consumer Disclosure Form and as authorized by the Dodd-Frank Act, has a unique opportunity to improve transparency for borrowers by requiring full disclosure of costs incurred for appraisal services and costs for appraisal management services. The CFPB has issued several drafts of the proposed Consumer Disclosure Form. We applauded a recent draft that was posted to the CFPB website for review in February, which includes clear disclosure of any fee paid to a “Local Appraisal Company” and to an “Appraisal Management Company” (“AMCs”) (found in both the “Hemlock” and “Butternut” versions).

### Part 3. Legislative Reform Options

As Congress reviews appraisal issues, we 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 with those of other industries in the real estate and mortgage sectors. One model to turn to is the National Mortgage Licensing System (NMLS), which is a cooperative amongst state agencies overseen as a last resort by the Consumer Financial Protection Bureau (CFPB).**

Comments: This is not a proposal to turn the appraisal regulatory structure over to a self-regulatory organization (SRO). SROs typically mean a regulatory scheme 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).

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 regime 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 after 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.

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<sup>22</sup> See “NAR Survey Shows HVCC Impacting Housing Markets,” available at [http://www.realtor.org/wps/wcm/connect/b83165804ef0b3338f18af2db4a1e62f/government\\_affairs\\_hvcc\\_research\\_results.pdf?MOD=AJPERES&CACHEID=b83165804ef0b3338f18af2db4a1e62f](http://www.realtor.org/wps/wcm/connect/b83165804ef0b3338f18af2db4a1e62f/government_affairs_hvcc_research_results.pdf?MOD=AJPERES&CACHEID=b83165804ef0b3338f18af2db4a1e62f)

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 was subsequently 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 state's requirements. Unlike the appraisal regulatory structure, the NMLS has a common application protocol which is accessed by all of the applicable state licensing authorities.

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 state regulatory information-sharing is not unique to appraisal, but is a widespread problem with many industries. The NMLS has addressed this by offering a solution that can be used by multiple industry regulators.

Lastly, should the NMLS fail in its responsibilities to manage appraisal oversight, the CFPB could 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.

**2. Congress must protect the independence of the appraisal standards-setting process and require that appraisal standards for federally related transactions be issued by an entity that does not directly or indirectly develop or offer education to appraisers.**

Comments: Standards-setting organizations typically go to great lengths to protect the independence of the standards-setting process. However, the decision now before TAF to enter into competition with private education providers would jeopardize the independence of this process, as changes made to standards may have additional motivations beyond those serving the profession or users of professional appraisal services. It is worth noting that TAF is not the only appraisal standards-setting organization in the world. In fact, the International Valuation Standards Council, based in London, produces the International Valuation Standards, which are adopted in more than 70 countries and are required for Appraisal Institute members conducting appraisal work internationally. In contrast to TAF, the IVSC does not currently directly or indirectly develop education for appraisers<sup>23</sup>. This is similar to other standards-setting organizations such as the Financial Accounting Standards Board and the International Accounting Standards Board, both of which also restrict them in the area of direct education.

**3. Congress must establish limitations around the Appraisal Practices Board of TAF.**

- a. **No tax dollars should be used to fund this venture.**
- b. **Voluntary guidance should be just that – voluntary.**
- c. **States should be restricted from codifying voluntary guidance into state law or regulation and the Appraisal Standards Board should be prohibited from specifically referencing works of the Appraisal Practices Board within USPAP.**
- d. **Establish meaningful oversight over the de facto regulatory actions of TAF.**

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<sup>23</sup> “Tom Boyle suggested a new project relating to real estate and the misunderstanding of nonconforming uses and the highest and best use principle. However other Board members considered that this would bring the IVSC into an educational role, which is not its remit.” From Minutes of the Meeting of the IVSC Standards Board Held in Hong Kong on 3 November 2011. Available at: [http://www.ivsc.org/meetings/2011/1103/sb/minutes\\_ivsb\\_20111103.pdf](http://www.ivsc.org/meetings/2011/1103/sb/minutes_ivsb_20111103.pdf)

Comments: The prohibition of treating voluntary guidance as compulsory should apply to the Appraisal Practices Board and any “Advisory Opinions” or “Frequently Asked Questions” published by the Appraisal Standards Board. Already, at least seven (7) states have inappropriately adopted Advisory Opinions and Frequently Asked Questions issued by the Appraisal Standards Board into their regulations; even though both clearly state that they are to be voluntary and to be used for information purposes only. Barring action by Congress, a similar course has been laid out for the Appraisal Practices Board.

- 4. Congress should reiterate that TAF does not have legislative authorization in the area of “methods and techniques” and “appraiser education.” Congress should not allow TAF to abuse the authorities granted to it for appraisal standards and qualifications, nor should TAF be allowed to compete with private education providers in the area of appraisal methods and techniques.**

Comments: There is a precedent for Congress to establish limitations in the area of education for private organizations that have direct authorizations from Congress. When it authorized the National Mortgage Licensing System, Congress established a limitation for the NMLS not to directly or indirectly develop or offer any qualifying or continuing education to those whom they oversee<sup>24</sup>. This is an appropriate comparable to the situation involving TAF, not just because it maintains a Course Approval Program that enables education providers to seek a single approval of education in all 50 states, but also because of the imprimatur as “the source” for appraiser standards and qualifications. We encourage Congress to enact similar parameters for the appraisal profession.

- 5. Congress should establish laws that empower state appraisal boards to do thorough and fair investigations and to prosecute meaningful complaints involving appraisers. Further, Congress should ensure that appraiser licensing fees are used by state appraiser regulatory agencies for appraiser oversight and enforcement through dedicated funds.**

Comments: Often, appraiser licensing fees are swept by state governors to help fill budget shortfalls or support non-appraiser oversight functions. Over the past year, the Appraisal Institute led an effort in the state of Maryland to dedicate appraiser licensing fees for appraiser oversight and enforcement. We have established model legislation for other states – approximately 15 – that are at risk of having funds swept for other uses.

- 6. Authorize Fannie Mae, Freddie Mac and other agencies, such as the Federal Housing Administration and the Veterans Administration, to halt purchase or guarantees of loans in states that maintain deficient appraiser regulatory regimes. This would serve as a strong incentive for states to maintain meaningful appraiser oversight and enforcement systems.**

Comments: Today, the ASC has the authority to “de-certify” a state appraiser regulatory structure if it finds states are not able to enforce Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989. The ASC has never used this authority for a variety of reasons. The Dodd-Frank Act authorized the ASC to establish intermediate sanctions, such as fines and suspensions. To date, it has not established any policies in this area.

- 7. 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.**

Comments: 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

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<sup>24</sup> The SAFE Act limits the National Mortgage Licensing System established by the CSBS from directly or indirectly offering education for qualifying or continuing education for mortgage originators. See 12 U.S.C. 5104(c)(3) [http://www.law.cornell.edu/uscode/html/uscode12/usc\\_sec\\_12\\_00005104---000-.html](http://www.law.cornell.edu/uscode/html/uscode12/usc_sec_12_00005104---000-.html).

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 can 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.

With regard to appraisal procurement, we encourage Congress to:

**1. Eliminate the Section 1122(d) of Title XI of FIRREA regarding member if nationally recognized professional appraisal organizations**

Comments: This would eliminate one more requirement imposed on lenders, while promoting professional development and participation in ethics and counseling programs that serve as additional layers of oversight and enforcement.

**2. Monitor the expected proposed rule from the Consumer Financial Protection Bureau on the Consumer Disclosure Form regarding implementation of Sec. 1475 of the Dodd-Frank Act, which authorizes the separation of appraisal and appraisal management company fees.**

Comments: We believe that the separation of appraisal and appraisal management company fees is a central component of efforts to improve appraisal quality. We hope the upcoming proposed rule from the CFPB provides for a separation of the Appraisal and Appraisal Management Company fees with a requirement for its disclosure. Barring this, we urge Congress to utilize its oversight function in this area.

**3. Monitor the implementation of the Interim Final Rule on Truth in Lending/Appraisal Independence.**

Comments: We also believe that it is central to the related provision in Dodd-Frank requiring the payment of customary and reasonable fees to appraisers. In this regard, we also call on Congress to utilize its oversight functions should a final rule regarding appraisal independence by the Consumer Financial Protection Bureau fail to commence in the coming year. We believe that Congress should demand that the CFPB issue a final rule that makes consistent the two presumption of compliance regarding compliance with customary and reasonable fee requirements.