



**National Association
of Home Builders**

Testimony of Ed Brady

**On Behalf of the
National Association of Home Builders**

Before the

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

Hearing on

**“Modernizing Appraisals: A Regulatory Review and the
Future of the Industry”**

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

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

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

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

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

NAHB Activities

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

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

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

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

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

Overview

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

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

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

Other challenges facing the appraisal industry include shortcomings in appraiser training and experience in dealing with new construction and green building. There is insufficient new construction, energy efficiency and green building data available to appraisers. Further, current

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

Current Challenges and Recommendations

Federal and State Oversight Is Complex and Flawed

Federal Regulatory Oversight

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

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

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

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

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

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

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

State Regulatory Oversight

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

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

Structure

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

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

Dedicated Resources

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

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

Governance

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

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

Standardization

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

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

Communication

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

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

Inconsistent Standards

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

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

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

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

Inaccurate Appraisals for New Construction

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

Appraiser Experience and Training

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

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

Inadequate Data

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

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

Valuation of Green and High Performance Properties

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

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

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

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

Establish a Workable Appraisal Appeals Process

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

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

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

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

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

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

“(c) EXCEPTIONS.—The requirements of subsection (b) shall not be construed as prohibiting a mortgage lender, mortgage broker, mortgage banker, real estate broker, appraisal management company, employee of an appraisal management company, consumer, or any other person with an interest in a real estate transaction from asking an appraiser to undertake 1 or more of the following: [emphasis added]

- (1) Consider additional, appropriate property information, including the consideration of additional comparable properties to make or support an appraisal.
- (2) Provide further detail, substantiation, or explanation for the appraiser’s value conclusion.
- (3) Correct errors in the appraisal report.”

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

“Consistent with its policies and procedures, an institution also may request the appraiser or person who performs an evaluation to:

- Consider additional information about the subject property or about comparable properties.
- Provide additional supporting information about the basis for a valuation.
- Correct factual errors in an appraisal.”²

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

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

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

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

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

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

² 75 FR 237 (December 10, 2010) p. 77457.

³ FHA Single Family Housing Policy Handbook 4000.1 Section II.A.3viii.

⁴ VA Circular 26-03-11, "New Procedures for Improving Communications with Fee Appraisers and Streamlining Reconsiderations of Value" (December 22, 2003).

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

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

Conclusion

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

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

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