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WHAT'S YOUR HOME WORTH? A REVIEW OF THE APPRAISAL INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON HOUSING,
COMMUNITY DEVELOPMENT,
AND INSURANCE

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTEENTH CONGRESS

FIRST SESSION

JUNE 20, 2019

Printed for the use of the Committee on Financial Services

Serial No. 116–34

U.S. GOVERNMENT PUBLISHING OFFICE
39–495 PDF WASHINGTON : 2020

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WHAT'S YOUR HOME WORTH? A REVIEW OF THE APPRAISAL INDUSTRY

Thursday, June 20, 2019

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

The subcommittee met, pursuant to notice, at 2:08 p.m., in room 2128, Rayburn House Office Building, Hon. Wm. Lacy Clay [chairman of the subcommittee] presiding.

Members present: Representatives Clay, Sherman, Beatty, Green, Maloney, Vargas, Tlaib, Axne; Duffy, Luetkemeyer, Huizenga, Tipton, Zeldin, Rose, Steil, and Gooden.

Chairman CLAY. The Subcommittee on Housing, Community Development, and Insurance,will come to order.

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Also, without objection, members of the full Financial Services Committee who are not members of the subcommittee are authorized to participate in today's hearing.

Today's hearing is entitled, "What's Your Home Worth? A Review of the Appraisal Industry."

Our last Housing Subcommittee hearing examined the state of minority home ownership and provided us with additional data, research, and background on the impact of home ownership on the racial wealth gap. This hearing is a follow-up as we explore the racial wealth gap in the context of inaccurate appraisals.

I stress that we look forward to working on structured policy solutions because we are, at our core, an optimistic nation. We fix problems. And I invite all of my colleagues to come together and work to find solutions to make the appraisal process more equitable to every American community.

While this hearing will touch on a number of critical topics affecting the industry, such as the de minimis threshold, appraiser independence, and the role of technology in appraisals, we would be missing the mark if the disparity in appraisals was not part of today's discussion.

For many Americans, the purchase of a home is a gateway to financial security and wealth, but if your path to growth is blocked by an inaccurate or skewed appraisal because you are living in the wrong ZIP Code, you are stifled. And in my district, if you are a black person in north St. Louis, north of Delmar Boulevard, you may have more reasons to worry. The Greenlining Project noted in their 2018 St. Louis metro report that the current framework gives the appraiser tremendous discretion. Appraisers decide the significant neighborhood parameters and physical boundaries that, although may appear racially neutral, can at times serve as a racial or class boundary.

The undervaluation of homes in minority communities nationwide creates an appraisal gap, which can effectively limit mortgage lending in specific geographic areas. In a typical lending scenario, the appraisal is lower than the real value of the home because there are additional costs to bring the home up to code in distressed and disinvested neighborhoods.

In a neighborhood in my district called the Greater Ville Neighborhood, for example, say you seek to purchase a home for, say, $35,000, and provide an additional $50,000 for rehabilitation of the home. However, the home only appraises for $70,000, far less than the $85,000 needed to purchase and renovate. Because of this appraisal gap, the loan is denied. Consequently, homes in impacted communities stay vacant and fall further into disrepair. Families are unable to become homeowners. It becomes an unending cycle and the racial wealth gap is further exacerbated.

I look forward to hearing from the witnesses today about solutions. All hardworking Americans deserve the opportunity to achieve the American Dream of home ownership.

And at this point, I will recognize the ranking member of the subcommittee, my colleague and friend from Wisconsin, Mr. Duffy.

Mr. DUFFY. Thank you, Mr. Chairman.

And I want to thank you for holding this hearing today. I want to also thank our panel for being here as well. I'm looking forward to a robust discussion on some of the issues you all see in the industry, and solutions that we can take as a Congress to remedy those problems that you discuss today.

I want to also get your input on a bill that Mr. Sherman has introduced, his appraisal certification bill, which I have been working with him on as well. A common concern I hear from the appraisal industry is the lack of appraisers nationwide. It is definitely a problem in rural areas, which gets exacerbated by the distance that the already limited number of appraisers have to cover by the drive time to go from community to community in rural America.

I look forward to working with Mr. Sherman on this bill on the standardization of the qualifications requirements for appraisers to evaluate loans backed by the FHA, VA, USDA, Fannie Mae and Freddie Mac. I have a few suggested changes, but hopefully this will open up some of the licensed appraisers who currently cannot appraise properties related to these programs.

I have had the opportunity to sit down with Mr. Clay, and we have discussed the issue of appraisals one-on-one. And miraculously, we are not too far apart, which would be shocking to some people as they evaluate the Congress these days.

I think we all learned in the 2008 crisis that there were overvaluations and there were undervaluations in some neighborhoods, and I don't think we want to go back to a cycle where we are not accurately appraising homes and their values.

I want to mention a recent legislative change that I think is helping people who live in rural areas, such as my constituents in central and northern Wisconsin, which I believe was in Senate bill 2155, that allows for rural properties worth less than $400,000 to forego the appraisal requirement. I also want to stress that you can still get an appraisal if you think the home is worth a different value; it is just not a requirement under the law. Now, I know that has created some concern in regard to how that has been interpreted and an expansion of that S.2155 by the regulators. Maybe we can discuss that further today.

Lastly, I want to bring up technology and how it can help reduce cost and speed the time it takes to buy a home, particularly utomated valuation models or computerized models that help determine worth of a property using this AVM technology. I am not saying this is for everyone, but they are being utilized by many of the industries to help expedite the closing process for those who may not have access to appraisals, such as what we have in northern Wisconsin.

The digitization and development of large troves of data holding millions of property records has also helped develop algorithms and streamline valuations. At the end of the day, we also have to make sure people still have the option to get a physical appraisal for any modifications or additions they have made to their home. In certain markets, physical appraisals may still not be necessary, but you have to look at each property and what it offers in regard to its value, whether it is the lot size, its amenities, its age, its roof, its new kitchen, maybe its invisible fence. I don't know if that adds any value to a place or not. But we do know that eyes on properties also provide probably the best insight into the value of that property.

So, I am looking forward to your testimony today. I want to thank you all for being here and I am looking forward to your recommendations for what this subcommittee should do, moving forward.

I yield back.

Chairman CLAY. I thank the ranking member.

And I now recognize the gentleman from California, Mr. Sherman, for 1 minute for an opening statement.

Mr. SHERMAN. Thank you. There is no more important day in the economic life of a family than the day they buy a home. Appraisers play an important role in that. I have a bill to change the rules a bit on FHA appraisals, to bring them more in line with those appraising for loans by Fannie Mae and Freddie Mac, and to deal with the backlog that we are experiencing.

And I look forward to learning from our witnesses how the appraisal process can be speedier, whether it is an FHA, GSE, or otherwise outside governmental involvement loan, and how we can keep costs at a reasonable level.

With that, I yield back.

Chairman CLAY. I thank the gentleman for yielding back.

And today, we welcome the testimony of Mr. David Bunton, president of The Appraisal Foundation; Mr. Stephen Wagner, 2019 president of the Appraisal Institute; Mr. Jeff Dickstein, chief compliance officer of Pro Teck Valuation Services, on behalf of the Real Estate Valuation Advocacy Association; Mr. Andre Perry, the David M. Rubenstein Fellow at the Metropolitan Policy Program, housed at the Brookings Institution; and Ms. Joan Trice, founder of the Collateral Risk Network.

Witnesses are reminded that your oral testimony will be limited to 5 minutes.

And, without objection, your written statements will be made a part of the record.

We will start with Mr. Bunton.

You are now recognized for 5 minutes to give an oral presentation of your testimony. You may proceed.

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

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

By way of background, I have served as the senior staff member of the Foundation for the past 29 years and prior to that, I had the privilege of serving as a senior congressional staff member for a dozen years.

Let me begin with a few words about who we are and what makes us different. We are a nonprofit organization founded 32 years ago before the enactment of the Financial Institutions Reform Recovery, and Enforcement Act of 1989 (FIRREA). We are not an advocacy group. We are not a trade association. We don't have any individual members. Rather, we are an umbrella organization composed of about 100 organizations and government agencies with an interest in valuation. We were created to foster excellence, unity, and trust in appraising. We are the private sector expertise in the real property appraiser regulatory system under Title XI of FIRREA. The Foundation does not have any regulatory authority, but we provide the tools for the regulatory community.

Specifically, we set the minimum education and experience requirements one must meet in order to obtain a State credential. We are the authors of the national uniform appraiser exams that are used by all 55 States and Territories. And, lastly, we are the authors of the generally recognized standards of conduct known as the Uniform Standards of Professional Appraisal Practice that all State-licensed and certified appraisers must adhere to. In addition, we have been a resource to numerous Federal Government agencies and currently have a cooperative agreement with the U.S. Department of the Interior.

Mr. Chairman, this hearing is of particular importance, and we applaud you for its timing. Thirty years ago, Congress passed Title XI of FIRREA, which created the appraiser regulatory system we have in place today. Unfortunately, that system is being significantly undermined by being circumvented. Let me explain why. Title XI contains a provision which allows the Federal financial institution regulatory agencies to exempt certain transactions from requiring an appraisal. As a baseline, in 1990, the financial institution regulators set that threshold at $50,000, with the exception of the Federal Reserve, which set it at $100,000.

Now, fast forward to today. According to the U.S. Consumer Price Index, that $50,000 threshold in 1990 would be about $99,500 today, and the $100,000 threshold would be about $199,000. But the current proposal by the financial institution regulators is to increase that threshold to $400,000.

The National Association of REALTORS reports that in April, the median price for an existing home was $267,300. But how can the baseline exemption threshold be 66 percent above the median sales price? Let's take a look at the enabling legislation, Title XI of FIRREA. Title XI contains 7,200 words. Ironically, the word "evaluation" appears one time, and that is in reference to a GAO study. Why is it only in there one time? That is because Congress viewed transactions below the threshold as exemptions to the process, not the common practice that it has become today.

So, today, instead of using competent individuals who have been trained, tested, and who adhere to standards and are accountable to a public board, evaluations can be performed by individuals who are not appraisers, who don't need to follow performance or ethical standards of conduct, and are not held accountable to a public board. Another workaround being embraced is automatic valuation models. Unfortunately, there are no quality control standards for these products and how they work is shrouded in secrecy.

What was put in place 30 years ago has been hollowed out, a shell of what the original congressional intent was. This could have serious ramifications for our Deposit Insurance Fund, the home buying public, and every U.S. taxpayer. As you know, borrowers are entitled to a copy of any valuation product ordered by a bank in conjunction with their loan. I think it is safe to say that most borrowers would be confused, not knowing the difference between a professionally performed appraisal and alternative higher risk valuation products.

Mr. Chairman, we look forward to today's discussion on this and other important valuation issues that you have raised: appraiser independence; impact of technology on appraising; diversity in the profession; and performing appraisals without bias. The testimony we have submitted contains 10 specific recommendations regarding this issue.

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

In closing, the title of this hearing begins with the phrase, "How much is my home worth?" We are simply requesting that the question be answered by a professionally trained appraiser. Thank you very much for the time.

[The prepared statement of Mr. Bunton can be found on page 32 of the appendix.]

Chairman CLAY. Thank you, Mr. Bunton, for your testimony.

Mr. Wagner, you are now recognized for 5 minutes.

STATEMENT OF STEPHEN S. WAGNER, 2019 PREIDENT, THE APPRAISAL INSTITUTE

Mr. WAGNER. Thank you. It is an honor to speak before the subcommittee today. My compliments to you for your timely consideration of real issues facing the appraisal profession and the impacts they have on consumers. And we are pleased with your direction, in terms of the FHA and registry fee bills currently under consideration. In addition, we applaud greater consumer transparency of fees associated with appraisal management.

Since the Great Depression, real estate appraisal has been an integral piece of the housing finance system used to ensure safety and soundness and protect the consumer. Today, the appraisal profession faces disruption on multiple levels, impacting practitioners and compounding difficulties in attracting the next generation of appraisers.

Altogether, the changes facing the profession are creating confusion and driving to undercut the critical role played by appraisers. Today's bank regulatory regime is promoting optionality to appraisal requirements, which is contrary to the original intent of FIRREA. These actions are sowing the seeds for future financial difficulties and that endangers consumers and taxpayers.

Specifically, the bank regulators are reversing course from a recommendation to maintain the residential appraisal threshold level and disregarding a measure enacted by the last Congress, purely with regulatory relief in mind. Further, we are witnessing battles between credit union and bank regulators, perpetuating a race to the bottom on risk mitigation. This is outrageous and should be concerning to all taxpayers and consumers.

2018 was the first year in more than a decade where we did not experience a bank failure. We have learned important lessons since the financial crisis, but measures taken for risk mitigation seem to be unraveling. Technology is being adopted and integrated by appraisers, but also is potentially disrupting fundamental practices within appraisal itself. The mortgage sector is utilizing waivers and hybrid approaches to speed up the loan-making and appraisal process.

There are standard of care questions here that remain outstanding and unresolved. We understand appraisers may need to adapt to new or hybrid approaches. However, we caution against the use of hybrids becoming a standard or the norm. Machines or secondary labor forces cannot replace the trained eyes of appraisers when it comes to risks associated with the property or positive attributes that contribute to value. There is nothing like observing the subject property to an appraiser or a trainee associated with the appraiser. A picture may be worth a thousand words, but it is not all of the words.

In addition, those inspecting properties for valuation purposes should have valuation training. If we are looking for ways to speed up the appraisal process, we suggest scrutinizing appraisal management companies, where we hear of delays related to both the ordering and review process. Lender and underwriter guidelines are also too often treated as rules. There needs to be more flexibility regarding the lender and underwriter guidelines to reduce second-guessing of appraisers. This will allow practitioners to wield their expertise in complex markets where sales data and activity may be limited or virtually nonexistent.

We also need a common-sense approach to courting appraisal services, particularly in terms of today's TILA–RESPA Integrated Disclosure Rule (TRID) requirements. Appraisers are often asked to bid on assignments without complete property information, which is understandable. However, we should acknowledge that once the appraiser sees the property, the ultimate scope of work could easily change. This can affect timing and fee. Therefore, the lender needs flexibility not found in today's zero tolerance environment.

Despite this, we see real opportunities ahead in addressing the concerns of the subcommittee and appraisers. We applaud the approach of the hearing today and the two bills before the subcommittee. We endorse full consumer transparency and separation of fees paid to appraisers and AMCs. Looking ahead, we urge this committee to explore other regulatory improvements, such as the establishment of a nationwide licensing system for appraisers to manage license applications, renewals, education records, and background checks, where required.

We look forward to working with you, Federal and State regulators, The Appraisal Foundation, and others to accomplish these goals. Thank you again, and I look forward to answering any questions you may have.

[The prepared statement of Mr. Wagner can be found on page 98 of the appendix.]

Chairman CLAY. Thank you, Mr. Wagner.

And, Mr. Dickstein, you are recognized for 5 minutes.

STATEMENT OF JEFF DICKSTEIN, CHIEF COMPLIANCE OFFICER, PRO TECK VALUATION SERVICES, ON BEHALF OF THE REAL ESTATE VALUATION ADVOCACY ASSOCIATION

Mr. DICKSTEIN. Good afternoon, Chairman Clay, Ranking Member Duffy, and members of the subcommittee. Thank you for the privilege of sharing the perspective of appraisal management companies at the subcommittee hearing today.

I have been a certified residential appraiser for 30 years, and I hold that credential in 17 different States. As chief compliance officer of Pro Teck Valuation Services, a national appraisal management company, I am responsible for the company's compliance with all Federal, State, and industry regulations.

I am here today representing the Real Estate Valuation Advocacy Association (REVAA), a national trade organization representing appraisal management companies (AMCs) and lender valuation providers. We appreciate the opportunity to provide insight into the appraisal industry from the perspective of the appraisal management company.

Passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, nearly a decade ago, has generated profound changes in the appraisal industry, just as Congress intended. AMCs are third-party service providers engaged by banks and nonbank lenders to work with appraisers on residential appraisals in compliance with Federal appraisal independence requirements. AMCs have been in existence since the 1960s. We did see growth in popularity among smaller and midsized lenders following the 2010 financial crisis.

Dodd-Frank also adopted several important consumer protections that REVAA supports, including but not limited to: maintain and promote appraisal independence; and to include AMCs within the scope of appraisal activities overseen by the Appraisal Subcommittee.

Dodd-Frank also set up a framework to amend FIRREA for voluntary State regulations of appraisal management companies. That vision has largely been realized as we approach the August 10, 2019, deadline. As of today, 49 States have implemented AMC registration programs, consistent with Federal law and rule. Massachusetts legislation is proceeding, and we do expect that to close. The only U.S. States and jurisdictions that are poised to opt out are the District of Columbia, Puerto Rico, Guam, the Virgin Islands, and the Northern Marianas Islands.

This Appraisal Subcommittee has begun reviewing State AMC licensing programs for compliance. Additionally, the national AMC registry is operating and will be fully populated by June 2020. We support legislation to grant the Appraisal Subcommittee discretion to amend AMC fees, if appropriate, to reduce some financial burdens. State regulators now provide oversight of appraisal management company activities in their States, along with the ability to investigate complaints and enforce violations.

REVAA supports several collaborative industry initiatives to make a real difference in attracting and training the next generation of appraisers, including possible addition of trainee appraisers to the national registry, The Appraisal Foundation AQB new education and experience requirements for new appraisers entering the field, as well as the creation of PAREA.

We also support industry efforts to recruit military veterans and other people to consider becoming appraisers, and REVAA strongly supports and would be willing to partner in any efforts to help sustain and diversify the appraisal profession. REVAA feels strongly that the future of appraisal needs to retain a human component, which is why we support the recruitment of new appraisers to help revitalize the profession for the next generation. The future isn't going to be solely reliant upon new technologies and data. Modernization won't replace appraisers. It will complement the appraiser's role in utilizing their experience, education, and local market knowledge to analyze the subject property, and to develop a credible opinion of value.

Beyond appraisals, there are a wide range of valuation products that can be available to financial institutions, mortgage companies, investors, and others making real estate collateral decisions: AVMs; evaluations; and hybrid, or desktop appraisals. REVAA supports the use of these products for permitted purposes. We do recognize that these products are not appropriate for all collateral valuation decisions when a complete full appraisal by a credentialed appraiser is warranted.

REVAA appreciates the opportunity to review the November 2018 report by the Metropolitan Program at Brookings. The information has been shared with our members, and we continue to review and assess the conclusions contained in that report. AMCs do employ many controls to ensure that appraisers and AMCs do not engage in any discriminatory behavior.

As we look forward to discussing the future of the industry, constructive dialogue and collaboration must continue. In that effort, REVAA fully respects and requests that Congress: pass H.R. 2852, the Homebuyer Assistance Act of 2019, which would permit licensed real estate appraisers to perform FHA appraisals; pass legislation to permit States to report appraiser trainees to the Appraisal Subcommittee register; pass legislation to grant regulatory flexibility to the subcommittee regarding AMC fees; and support the registration oversight of AMCs in all States, Territories, and the District of Columbia.

That is my statement. Thank you.

[The prepared statement of Mr. Dickstein can be found on page 56 of the appendix.]

Chairman CLAY. Thank you so much, Mr. Dickstein.

Mr. Perry, you are now recognized for 5 minutes.

STATEMENT OF ANDRE M. PERRY, DAVID M. RUBENSTEIN FELLOW, METROPOLITAN POLICY PROGRAM, THE BROOKINGS INSTITUTION

Mr. PERRY. Thank you, Chairman Clay, and Ranking Member Duffy. Home ownership lies at the heart of the American Dream, representing success, opportunity, and wealth, as it should. The equity that typically comes from owning a home may ultimately open a business, send a child to college, or start a family.

The data I will present today will show that racism is at the present day extracting money from homeowners in black communities to a painful sum of $156 billion, keeping those who are striving for the American Dream from actually reaping its benefits.

We have known for some time that racism limited black people's housing options in ways that lowered the values of their home. De jure and de facto segregation as well as racially restrictive housing covenants prohibited blacks from buying in certain areas throughout the 20th Century. Racially biased, federally backed redlining isolated people in neighborhoods that saw lower levels of investment than their white counterparts.

My study that is presented in the written testimony shows that in the average U.S. metropolitan area, homes in neighborhoods where the share of the black population or the share of the population that is at least 50 percent black are valued at roughly half the price as homes in neighborhoods with little to no black residents.

Many assume the 50 percent price difference isn't about racial bias. They attribute lower prices to inferior housing, underfunded schools, and crime. My colleagues—Jonathan Rothwell at Gallup, and David Harshbarger, also with the Brookings Institution—and I tested those assumptions. We examined homes of similar quality in analogous neighborhoods with the exception of racial demographics to make an apples-to-apples comparison between black and white neighborhoods. What we found astounds. Differences in home and neighborhood quality do not fully explain price difference. After controlling for factors such as housing quality, education, crime, and other influences, homes in majority black neighborhoods are worth 23 percent less. That amounts to $48,000 per home, on average. Nationally, that is a whopping $156 billion that homeowners lost because their homes were not priced at market rates.

The study also found that areas that had high devaluation exhibited low economic mobility for its residents. Racial bias reflected in the pricing and price is robbing money that people can use to uplift communities. The valuation means municipalities with a significant percentage of African Americans lose tax revenue that could be put towards government services and infrastructure. Take St. Louis, for example. Black neighborhoods in this metro area see a 28-percent price difference, amounting to a $30,000 loss per home. In the Houston metro area, there is a 27-percent difference, resulting in a $53,000 loss. The Columbus, Ohio, metro area sees homes devalued by 21 percent, on average, or $23,000. And in the metro area with the largest majority black City in the nation, Detroit, Michigan, there is a 37-percent difference, resulting in a $28,000 in loss equity per home.

Let's put that $156 billion in perspective: $156 billion could have started 4.4 million black-owned businesses, based on the average amount of funds blacks use to start a company; or it could have paid for 8.1 million 4-year degrees, based on the average tuition of public universities in 2016. These are real wealth-building opportunities that could have catapulted the black population to greater heights. Also, $156 billion could have replaced pipes in Flint, Michigan, 3,000 times over, and paid for nearly all of the damage caused by Hurricane Katrina. That $156 billion is more than double our country's efforts to combat the opioid crisis.

In effect, bigotry imposes a black tax on residents of majority black neighborhoods while throttling opportunities for economic mobility. Let's be clear: Discrimination in home valuations impacts everyone. White and Latino homeowners in black neighborhoods are also losing equity as well. There are exceptions. Madison, Wisconsin, realizes a 70-percent added value in black neighborhoods, and there are others.

Clearly, we still need better policies to give homes in black neighborhoods their proper value. Assessment tools are not neutral. People are not neutral. You will hear the argument that we need more people. People are part of the problem. But what is clear is that black people are not part of the problem. I often say there is nothing wrong with black people that ending racism can't solve. Whether we go to more automated systems or more people, we still must have a neutral arbiter that will look at these valuations critically.

[The prepared statement of Mr. Perry can be found on page 68 of the appendix.]

Chairman CLAY. Thank you, Mr. Perry, for your testimony.

And Ms. Trice, you are recognized for 5 minutes.

STATEMENT OF JOAN N. TRICE, FOUNDER, COLLATERAL RISK NETWORK

Ms. TRICE. Chairman Clay, Ranking Member Duffy, and members of the Subcommittee on Housing, Community Development, and Insurance, thank you for the opportunity to share my thoughts regarding, “What is Your Home Worth? A Review of the Appraisal Industry.”

I am going to deviate a little bit from my written testimony that I submitted and just sort of do a summation, if I may, of what you have heard so far. The appraisal industry is quite complex, as you have learned by now. It is an incredibly important part of the housing finance infrastructure. And after the last hearing that we had in 2016, I had the pleasure of getting together with the Executive Council of the Collateral Risk Network, which is a group of chief appraisers, risk managers, real estate appraisers, and a few regulators that we put together in a room and just sat down with a white board and said, “Okay. What is our mission here? Let’s take a look at a postmortem of the last crisis. How did we get here? Is our current regulatory structure actually meeting the needs of a modern 21st Century housing finance system?”

And the guiding principle in all that was, let’s put together a plan that works best for the health, safety, and welfare of real estate finance. So what we came out with on the other end was a plan to consolidate, if you will, all of the different entities and regulators that impact and touch the appraisal process today.

And, hopefully, you all will remember me as the gal who created the spaghetti chart. If you are all a little confused as to how we operate, you should be. It is confusing to appraisers. It is confusing to regulators. It certainly has to be confusing to consumers. Today, housing finance is a lot more sophisticated than it was when I entered in 1981 at a savings and loan in Baltimore, Maryland. Today, we have a vibrant capital market that is much larger than it was pre-mortgage crisis. And yet today, I don’t see any progress towards appraisal independence, more credible appraisal reports, and we certainly aren’t seeing any regulation of even new tenets that we put into place with Dodd-Frank.

Our concern is that we do need to modernize. As Congressman Duffy pointed out, technology—and there is also lots to be discussed around data privacy; who owns the data? This real estate data is being input into models. Who is monitoring the models? We have had capital markets, long-term capital management. We had some world-class Pulitzer Prize-winning economists who built algorithms that were supposed to be genius. There is a great book called, “When Genius Failed.”

So, we have to be very careful about how we proceed forward when we are taking real estate data that begins with the appraiser, the boots on the ground, and carry it through the system. There are a lot of people who touch it. And in the end, we need to ensure that we are having credible appraisals performed by licensed, qualified local market experts. Thank you.

[The prepared statement of Ms. Trice can be found on page 80 of the appendix.]

Chairman CLAY. Thank you so much, Ms. Trice.

And let me thank the entire witness panel for your testimony.

We will now move to the 5-minute phase of questioning of the panel, and I will start with 5 minutes.

Let me start with Mr. Perry. Mr. Perry, I have read your study and heard your testimony. Can you offer up to this committee some solutions to how we get to equitable evaluation of home values?

Mr. PERRY. First of all, again, thank you for having me. Something that is not mentioned enough, particularly in black communities, is there needs to be some type of micro-loan program so that people can actually keep their homes up-to-code and up-to-speed. Many, particularly black Americans suffer from the same financial insecurities just from the overall market. And so, when you don't have the discretionary resources to fix up your home, it is going to lag.

Chairman CLAY. Don't leave out the fact that also, when you go to a financial institution for a home improvement loan, your house is valued less.

Mr. PERRY. I was going to get to that. But the devaluation of your property impacts all of those things, your ability to get an additional loan.

What was also clear is the consistency in the data of how the valuation really hit black communities. And I am actually very interested in hearing the rest of the panel's perspective on training because it is almost as if people look at black communities and they see worse education, they see more crime, they see worse property, so when the assessments come out, they are much lower. But from our vantage point, using the data that we have, we can clearly see if you theoretically helicoptered one property into a white neighborhood, it would increase in value.

Chairman CLAY. Let me go to Ms. Trice, because you touched on this somewhat. How should the reporting or the appraisal process change to improve on appraisals and weed out the individual racial biases? How could we address that?

Ms. TRICE. That is a complex question, and it is going to take a complex answer. But I will try to keep it as simple as possible.

I think we need to actually go back to fundamental appraisal 101. There are three approaches to value: the cost; the income; and the market approach. Today, we have a system where the regulators have actually devolved the process to a single leg of that three-legged stool, and it is the sales price approach to value.

I respectfully submit that the codified definition of market value needs to be modernized. And there is a lot of confusion even amongst appraisers on price versus value. As Warren Buffett said, "Price is what you pay; value is what you get." It is a pretty simple concept if you look at it from that context and that construct.

So I think we have to have better education, better trained local market experts, and less reliability on automated tools because there is going to be disparate treatment. And that is really my biggest concern is that if we remove and waive appraisals for people with high credit scores, we are disparately mistreating, I think, the affordable housing sector.

Chairman CLAY. Thank you.

Mr. Wagner, I have a draft of a bill that would provide the AFC with increased flexibility to set fees assessed on AMCs and increase flexibility in allocating the proceeds of such fees. It would also allow trainee appraisers to be added to a national registry.

Based on your experience as an appraiser, what do you believe are the root causes of the devaluation of minority homes, and what do you believe the solution should be?

Mr. WAGNER. First of all, Congressman, I appreciate the question and empathize with your concern relative to the communities that you have mentioned. It is actually a concern that is really larger than the realm of appraisal. It involves, I think, lending in general.

Having said that, I will emphasize that a residential appraiser is bound by standards, and cannot consider racial, ethnic, or income makeup of a particular neighborhood or community. And this is a complex challenge. But perhaps a lending program similar to what is under development in Detroit and St. Louis, greenlining, might be helpful.

And, furthermore, I would like to add that we look forward to being a part of the conversation with you and your staff on this complex issue.

Chairman CLAY. I thank you for your response. My time has expired.

I now go to Mr. Duffy.

Mr. DUFFY. Thank you, Mr. Chairman.

Mr. Perry, if you would just kind of dig into this a little bit for me so I can understand. Do we have in predominantly African-American communities non-African Americans doing the appraisals in your study?

Mr. PERRY. Yes. I mean, the industry is largely white. I want to say it is roughly 90 percent white in terms of appraisals. And that is part of it. We do know that representation matters in terms of how you view or measure something. And so, in any kind of measurement, who is doing the measuring matters.

Mr. DUFFY. If you have ever tried to refinance or you have tried to sell a home and your appraisal comes in under the value that you think it should be, there is nothing more frustrating that will anger you more than that. I am speaking from experience on that myself.

Is it a chicken or an egg situation? Do we have comparable pricing that doesn't work? I guess if we have sales of comparable properties at one level and then the appraiser is coming in at a lower level, that is a problem, or we just fundamentally have lower valuations and lower sale prices?

Mr. PERRY. I will echo Mr. Wagner's comments that this is also about lending practices, real estate agent practices, and appraisal. So, it is all combined. But what is clear from the research is that we can actually control for neighborhood conditions, the housing structure. We can find similar homes across-the-board. And the only difference is the concentration of black folks around that home that accounts for the price.

So, all of those factors, there is some type of racial bias occurring. It is not just appraisals, but it is also in the lending and real estate agent practices. But what is easy to do, and I encourage the industry to at least have a neutral—an empirically rigorous database so that they can then say, okay, how off are our assessments? Because clearly, something is off kilter.

Mr. DUFFY. And I look forward to working with you. I know Mr. Clay does as well. This shouldn't happen.

But just to make another note, if you drop my house from Wausau, Wisconsin, to somewhere out here, it would probably go up 4 times in value myself.

Mr. PERRY. But if you—

Mr. DUFFY. Neighborhood to neighborhood, I know your point, but I wanted to make the point that I would be a lot wealthier.

Quickly, how many of you are appraisers? Some in the background too are all raising their hands. I have two appraisers, three appraisers on the panel. Obviously, we are using more technology. And I guess I am not opposed to technology, but I have a hard time seeing how technology and data can replace an appraiser going to my property and looking at all the intricacies of what my property has in regard to its value.

Any concerns on the panel if we are going to a far more data-driven non-human set of policies, and is that good for our housing industry, and can we get the wrong valuations? And when we get the wrong valuations, bad things happen, as we saw in 2008. I am asking a lot of questions. So, Mr. Wagner, if you want to go first, raise your hand.

Mr. WAGNER. Thank you, Congressman.

You know, you bring up some interesting points there. In some instances, technology with regard to, say, automated valuation models (AVMs), might have some place relative to very homogeneous type of housing and so forth where there are not a lot of differences. But also, with respect to AVMs, they are oftentimes based on a lot of, say, assessment record data, which may be inaccurate.

Mr. DUFFY. Mr. Wagner, with regard to that data they are using, the appraisal on my home could have been how long ago when I actually had an appraiser there? If you were in a close timeline, that might make some sense, but if the last appraisal was 8 years ago, a lot of things happen to a home in 8 years.

Again, if you are close in time, I might say, "Listen, I know you want your 600 bucks, but we just did an appraisal last year; come on, don't make me do another one."

Five years ago, 8 years ago, I don't see how data replaces the role of a man or a woman coming to my property.

Mr. WAGNER. And I agree with you, because the market conditions change and properties change. So a lot of times the data is imperfect at best. At the end of the day, there is nothing better than an appraiser laying his eyes on the property. I can't tell you the number of times that I have changed my mind after I have looked at the comparables, I have looked at the subject, and so forth.

Mr. DUFFY. I just noticed my time is up, but to save a few bucks to get this wrong has devastating impacts on everybody in America in a profound way. And to save a few dollars to potentially have a massive crisis like we had in 2008, I don't think is actually worth it. I would think we should err on the side of safety as opposed to technology and a few dollars saved in a closing.

With that, Mr. Chairman, my time is up, and I yield back.

Chairman CLAY. Mr. Bunton, you looked like you wanted to say something. Go ahead.

Mr. BUNTON. Thank you, Mr. Chairman.

At least for now, anyway, computers don't buy houses, people do. And computers are very good at coming up with tangible, the square footage, the number of bedrooms and bathrooms and all that. But it is a uniquely human quality. There are a lot of intangibles. Call it curb appeal, call it whatever you want, but that is going to impact on whether or not that house sells. So, AVMs are a great tool, but appraisers should be involved in the process.

Chairman CLAY. Thank you, Mr. Bunton.

I now recognize the gentleman from California, Mr. Sherman, for 5 minutes.

Mr. SHERMAN. One of the two bills we are focusing on in this hearing is the Home Buyer Assistance Act, and it deals with the requirements for an FHA-financed home. Over 83 percent of the FHA home purchases made last year were obtained by first-time home buyers, and one-third of all FHA loans were obtained by those in minority households. So, we have a real interest in making sure that the FHA process is one that works well.

Fannie Mae, Freddie Mac, the other major process, allows for either licensed or certified appraisers, and yet the FHA continues to require certified appraisers. Now, it is my understanding that this requirement goes back to the days when there were no national standards for licensed appraisers, but this committee took action to pass the Housing and Economic Recovery Act, which now imposes minimum national standards on licensed appraisers.

So, we have a circumstance where FHA is requiring certified and the other major finance agencies are saying licensed or certified. And I have a bill to correct that. I want to focus on that the bill is supposed to deal only with single family homes. You can make an argument that if one is financing a very complex property, that one should go with a certified appraiser.

I will ask Mr. Wagner and Mr. Dickstein, who both represent the industry participants here, is a licensed appraiser competent to appraise for FHA purposes the purchase of a single family home? Put another way, should we require a certified appraisal for the GSEs, Fannie and Freddie? Mr. Wagner?

Mr. WAGNER. I appreciate the question, Congressman. And I think the answer is yes, I think that licensed appraisers can do those appraisals as long as there is an education component because FHA requirements are over and above what you typically see for conventional type lending, the GSE type lending that you mentioned, or loan purchasing. So as long as that education component is there, we see an opportunity that is worthwhile.

Mr. SHERMAN. Mr. Bunton?

Mr. BUNTON. Yes. Our qualifications board has established qualifications to be a licensed appraiser for 2 or 3 decades, but with the Dodd-Frank Act in 2010, now that is the threshold, the floor. But we have felt all along that licensed appraisers should be able to perform residential lending for FHA and strongly support what you are doing.

The restriction on certified appraisers has really had a negative impact in rural America, where you had licensed appraisers who were only doing one or two appraisals a month. They let their license lapse because it wasn't worth it to go back and get that higher certification. So, this is good news.

Mr. SHERMAN. Do certified appraisers charge more?

Mr. BUNTON. I'm sorry. I didn't hear the question.

Mr. SHERMAN. If you are going to get an appraiser, you have a choice between a licensed one and a certified one. Does the certified cost more?

Mr. BUNTON. It shouldn't. No, no. The certified versus licensed has to do with the scope that you can appraise. In other words, you can appraise commercial properties, the value.

Mr. SHERMAN. And, obviously, if it is a complex commercial property, they would charge more. But to appraise the same house, it is the same fee?

Mr. BUNTON. Correct.

Mr. SHERMAN. And what does an appraiser need to do for an FHA mortgage beyond what they need to do for a Fannie or Freddie mortgage?

Mr. BUNTON. I am not competent to answer that one. One of the appraisers could do it.

Mr. WAGNER. Typically, the FHA appraisals involve more in the appraisal inspection process. They are looking for certain things, safe, sound, sanitary, with respect to the home and so forth. And they take into account and point out a number of issues that they see. So there is more to—

Mr. SHERMAN. So FHA just requires more work to be done, more things to be checked before you come in with that appraisal number?

Mr. WAGNER. I think that is a fair way to put it, sir.

Mr. SHERMAN. I yield back.

Chairman CLAY. Thank you.

I now recognize the gentleman from Colorado, Mr. Tipton, for 5 minutes.

Mr. TIPTON. Thank you, Mr. Chairman. And I thank the panel for taking the time to be here.

I would like to broaden out maybe some of the discussion a little bit that we are having here today. I come from rural Colorado. And we have a lot of our rural communities that obviously have some real challenges that they are being faced with in terms of even being able to find an appraiser to be able to come in and to actually be able to look at the property.

Under S.2155, which, just for clarification, was actually a House bill slightly modified that we should have been able to take credit for, when that was signed into law, we did have the provisions that were put in there in regards to the exemption with certain qualifications to try and be able to address that.

And I would just like to be able to hear maybe some of your thoughts on where some of that was right, maybe some of the shortcomings, your thoughts on S.2155, and did we do enough to be able to address some of the issues for appraisers? Mr. Bunton?

Mr. BUNTON. Yes, thank you very much. A couple of things regarding shortages in rural America, and there are underserved areas, no question. One of the things we are trying to do is have virtual training for appraisers. Instead of going out and finding a supervising appraiser, you could do it from your home, computer-based. Think of it like airline flight simulators and things like that. It is a work in progress. We hope to have it done in the not-too-distant future. But now, if you are in a rural county somewhere where you can't find a supervising appraiser, which is part of the qualifications process, you will be able to use this high-tech version. I think that will make a big difference as well.

We have also changed the qualifications to become a licensed appraiser and a certified appraiser where there are different pathways now, where you can do it through your experience, education in lieu of a bachelor's degree, an associate's degree. So we are allowing the pool of people to be larger who could actually get the credential from the State.

Mr. TIPTON. Great. Mr. Wagner, do you have any thoughts on that?

Mr. WAGNER. I do. And S.2155 was something that we supported. And the idea that there could be an exemption from getting an appraisal in a rural area if the lender had made contact with several appraisers and weren't able to locate somebody, that that possibility existed. We did support that. However, it really hasn't had that much of a chance to be tested yet.

And now the regulators are actually looking to increase from $250,000 to $400,000, which really ignores the whole appraisal aspect altogether at that point, as far as safety and soundness, consumer protection. So, we would advocate certainly that S.2155 gets its chance.

Mr. TIPTON. Any other thoughts on this?

Mr. DICKSTEIN. I would just like to add that we have seen comments from Freddie Mac, I believe at Ms. Trice's valuation expo conference a few times, a presentation where they have taken their appraisal submissions to their UCDP portal and put that up against mortgage submissions and stretched that out over time. And they have seen that there is some shortage in some areas, but it really is seasonally and that there is some correction based on the season. But we have seen some shortage at seasonal times.

Mr. TIPTON. Great. Just to be able to let a little bit of framework, part of my district has what is called the Four Corners area. It is where Utah, New Mexico, Arizona, and Colorado all come together. In each one of the States, within close proximity to each other, you have communities that are across State lines. And under current appraisal requirements, it is State by State to be authorized on that.

Mr. Wagner, maybe you could speak a little bit about maybe the possibility, the benefits or lack thereof of being able to have some kind of a national sort of appraisal rating?

Mr. WAGNER. Thank you for the question, Congressman.

We are in favor of looking at some sort of mortgage license—excuse me, some appraisal licensing type platform, a portal where appraisers could actually submit all of their applications, renewal applications, education records; if background checks were necessary, that as well. And we look at it as a win-win for all the stakeholders because, not only would that cut red tape for appraisers, because they have different requirements among the States and different timing among the States oftentimes for their licenses, but it would also make it easy access for the State regulators to pull down that information when application requests come in.

And what you are talking about in a proximity situation like that with Four Corners, oftentimes appraisers are licensed in multiple States. So, that would be a big benefit.

Mr. TIPTON. Thank you for that.

And, Mr. Chairman, Mr. Bunton had spoken to some ideas as well. We have a lot of our conversation, which is always framed typically around our urban areas, and I just want to really encourage our committee to remember that rural America plays a very important role in this economy as well and to make sure that when we are talking about appraisal, the access to be able to get homes, we do not leave out rural America as well.

Chairman CLAY. And I couldn't agree with the gentleman more. This subcommittee looks at all of America, rural, urban, suburban. So, thank you.

Mr. TIPTON. Thank you, Mr. Chairman.

Chairman CLAY. The gentleman from Texas, Mr. Green, who is also the Chair of our Subcommittee on Oversight and Investigations, is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman, and I thank the ranking member and the witnesses for appearing.

I would like to agree with the chairperson that we do look at all aspects of issues. A good many members of my family live in rural America, so I am greatly concerned about them.

But, today, permit me to say to Mr. Perry, Mr. Perry, I would have paid good money to hear your report. I am just blown away by what you said. And you are with the Brookings Institution, is that correct?

Mr. PERRY. That is correct.

Mr. GREEN. Okay. If you are on the panel and you are familiar with the Brookings Institution, would you just raise your hand? Okay. Everybody is familiar—all right. Everybody else out there, raise your hand? Brookings, okay. Everybody is familiar. Not for profit, doesn't take a position on issues but presents intelligence, facts, and what you have presented is astounding. Just for edification purposes, some things bear repeating: Homes of similar quality in neighborhoods with similar amenities are worth 23 percent less in majority black neighborhoods compared to those with very few or no black residents.

Now, at some point, we can say that this is a complex issue and I agree, but it can also be a complexion issue. There is something going on here that is very hard to deny, given the information that you have shared with us. I have in my office photographs of persons from hearings very similar to this. In fact, I brought a couple of photographs in today from a previous hearing where I had persons raise their hands when I asked a question. And one of these photographs has under it, "Ask me about this picture." It is my way of publishing beyond these hearings what takes place in these hearings.

So, this is going to be a photograph for my office. I will have under this photograph, "Ask me about this picture." I am sharing this with you because I want you to know this is a pretty important question for me, and if you care about your station in life as it relates to this picture, it may be important to you. Do you believe that invidious discrimination—"invidious" means harmful—plays a role in the devaluation of property in neighborhoods that are predominated with minorities but, more specifically, black people? If you do believe this, raise your hand. I want my staff who are recording this to be sure to get this picture. Would you raise your hand again, please? Only one person believes that invidious discrimination plays a role. So let me ask again for fear that you didn't understand.

If you think black people are being discriminated against when their property is being appraised, would you kindly raise your hand? One person on the panel. If you think that—for fear that I am not communicating well, if you think that black people are not being discriminated against when their property is being appraised, if you think they are not being discriminated against, kindly raise your hand. Okay. Hands now. We are getting some consternation, I see.

Yes, sir, Mr. Wagner?

Mr. WAGNER. Could you repeat the question? Could you clarify that for me a little bit more? Your question was, do we believe they are not being discriminated against?

Mr. GREEN. Let's do it again. I will give you a do-over. If you believe that black people are being discriminated against when their property is being appraised, not all, but in these neighborhoods where you have more than 50 percent of the neighborhood is black people, and the property values are similar to other—property is similar but the values are not? Do you think there is discrimination involved in this devaluation of that property? If so, raise your hand? One hand. All right. Well, the picture will be up for all to see, and I will probably bring it to future hearings. I will not let these things go. At some point, we have to deal with racism. We call it unintentional bias, and some of it is done with intentionality. So, this is my way of dealing with it.

I yield back the balance of my time. Thank you.

Chairman CLAY. The gentleman's time has expired.

The gentleman from Tennessee, Mr. Rose, is recognized for 5 minutes.

Mr. ROSE. Thank you, Mr. Chairman.

There is a broader conversation going on right now about potential housing finance reform. Most of the discussion over the past few years regarding housing financial reform has focused on the secondary market. However, it is important to also discuss the primary market. Not only do the originators of mortgages play an important role, but so do appraisers, given their important role in the origination process.

Do you think there are some potential changes to the appraisal regulatory structure that should be included in this effort? And I will start with Mr. Bunton on that.

Mr. BUNTON. Yes. I think, as I pointed out in my opening comments there, that we need to have professional appraisers determining what the value is of property that is the collateral for the loan. Somehow requiring the financial regulators to go back to using appraisers, to work with The Appraisal Foundation, we can come up with standards for evaluations as well as we have standards for appraisals. But, right now, they have developed a great big work-around, and they have circumvented everything that you all have put in place.

Mr. ROSE. Ms. Trice, would you speak to that?

Ms. TRICE. Gladly. We have spent a considerable amount of time devising what a new regulatory structure should look like. The appraisal is used not only in the origination, as you said, but also all the way through the system to the secondary market.

There are a lot of people who touch an appraisal along the way and rely on a credible appraisal report. I think today we are—FIRREA was probably the right thing at the right time. That was 1989. I think the most popular car in 1989 was an Oldsmobile Cutlass. If there is still one on the road today, it is probably being held together with duct tape. And I respectfully submit we have an outmoded, old, tired regulatory structure and that it is time for an overhaul.

Mr. ROSE. How important are accurate appraisals to ensure that federally backed mortgages, whether they be pulled in Ginnie Mae securities or into the uniform mortgage-backed security that Fannie and Freddie will be issuing, are quality credits?

Ms. Trice?

Ms. TRICE. The data today—I think that most people actually are going to find this a little astounding. There is less information on the collateral and the collateral value available to investors today than there was pre-crisis. I find that astounding. If you have ever watched, "The Big Short," you are, like, how did that happen? Well, we are doing it again. Today, in a credit risk transfer, the investor doesn't even get the property address, so how could they possibly do any sort of due diligence on the collateral valuation? They can't. They are completely—it is a blind bet. And so what the investor is relying on 100 percent is the full faith and credit of the United States, and that, my understanding is, we are trying to get away from a government backstop. But that implied guarantee is not allowing us to move into a more vibrant housing finance system, in my opinion.

Mr. ROSE. And I would ask all the panel this. To your knowledge, is there any reliable data that tells us whether the de minimis exception properties are being checked to be sure that there is real value there? In other words, is that de minimis exception being gained, if you will, and what risk do we see there? Yes, Mr. Bunton?

Mr. BUNTON. The valuations are being performed by nonprofessionals or can be performed by nonprofessionals. They don't have to adhere to a written set of standards, and they are not held accountable to a public board. So, if a homeowner has an evaluation below the threshold, hasn't complained about it, what recourse do they have? If it is an appraiser, you go to the appraiser board, so it is gaming the system. I think those were your words. I agree with you.

Mr. ROSE. All right. And then is there a danger that, without proper regulatory structure, appraisals could be gamed in order to comply with Fannie/Freddie conforming loan limits? Mr. Wagner, what is your opinion on that?

Mr. WAGNER. I think that if the de minimis is raised and use of evaluations increases, you are going to have increased risk as well because, at this point, as Mr. Bunton has said, the evaluations don't have to be done by anybody who subscribes to a strict code of ethics and standards.

Mr. ROSE. All right. Thank you.

I yield back.

Chairman CLAY. The gentleman's time has expired.

The gentleman from California, Mr. Vargas, is recognized for 5 minutes.

Mr. VARGAS. Thank you, Mr. Chairman.

I appreciate the opportunity to speak, and I appreciate you very much for having this hearing, and I also want to thank the ranking member. I want to ask a few questions along the line of my good friend, Mr. Green from Texas. I believe that there is discrimination. I don't think there is any doubt about that in housing. In fact, we have had redlining before. In fact, we hear all the stories. They are anecdotal, but someone is moving into the neighborhood. It is going to bring the property values down. I know that was the case when my family moved from one place to another. "Here come the Latinos." And so, I definitely think that there is some discrimination going on. Mr. Perry, you placed it at 23 percent less the valuation. Just out of curiosity, do you have any percentage for Latino, majority Latino neighborhoods?

Mr. PERRY. No, but we will be producing a report on majority brown cities as well.

Mr. VARGAS. Okay. I definitely think that is the case. I have to say that sometimes—I bought a number of properties in my day and still own a number of properties, and the appraisal sometimes works in your favor when it comes in low, too. It depends. I have bought a number of properties where they are in majority minority areas, and the appraisal comes in low, so you can negotiate the price down even further. You just have to put more cash into the deal, but it actually comes out in your favor. And if you have faith in that community and that neighborhood, the value is what you ultimately think it is. I agree with what Ms. Trice said, that is the value. The value to you is what you think it is going to be worth. And so I have done that a number of times, and I have come out more than okay.

So I will ask that question. It seems to me that you were saying that there is no discrimination, that there is no—that, to me, sounds so far off the ball that it is almost laughable.

Mr. Bunton, I will give you an opportunity to speak. Go ahead, sir?

Mr. BUNTON. Appraisals are reflecting what could be discrimination out there. Are homes selling for less in minorities areas? According to appraisers, they are, according to Mr. Perry's stats. But that is a reflection not on the appraiser. The appraiser should be reflecting what the market is. They don't make the market; they reflect it. Are people willing to pay less for minority neighborhoods? Apparently, that is the case.

Mr. VARGAS. I am not sure that they are not making the market, but I guess that is what I would argue. So, if the appraisal comes in lower, in fact, you can push the price down. I know I have done that a couple of times because I thought the appraisal was going to come in lower than it should, but I had cash to put into the deal. So I said, depending on the appraisal, and the appraisal came in low as I expected because of the neighborhood, then I was able to negotiate the price down in at least two instances because I thought this is what is going to happen. They are going to appraise this very low because of the neighborhood. I think the value is much higher because of location, location, location, and it worked out quite well for me. And so I do think that the appraiser—because the big deal with appraising, and I know you guys have mentioned it briefly—is comparables. They are always looking for the comps, what are the comps in the area. That is the big deal. But you also have to take a look at, what is the value? What do you feel it is worth? What is its proximity to downtown or whatever, saying it is around the bay or whatever it is? So I do think the appraisals do create part of the value of that neighborhood, and, again, I know that, in my own case, I have been able to negotiate what I think have been very good deals and sold them for very good profit because the appraisal was going to come in low because of what I thought was going to be discrimination.

Now, it might have been simple chance. I know it worked for me, but it seems to me that that is discrimination. Mr. Perry, you wanted to say something?

Mr. PERRY. I just want to add that we see this in cities where there is a large influx of white people coming into cities. They come in. Property values are very low. Within an instant, property values go up. And the research is pretty clear on this in terms of lending, appraisals, real estate behavior. We have cited discrimination at every turn. The price just reflects all of that and then some. So I don't think there is any question there is discrimination. We have concrete evidence, and I encourage people to read some of the review in the report that alludes to some of that, but there is discrimination. The housing market was predicated on suppressing black prices in particular areas. Those areas still exist, but more importantly, those behaviors are still there.

So, as long as you devalue black people, the tools you use will devalue black property.

Mr. VARGAS. I agree with you. My time has expired, but again, thank you very much.

Thank you, Mr. Chairman.

Chairman CLAY. The gentleman's time has expired.

The gentleman from Missouri, Mr. Luetkemeyer, is recognized for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

Mr. Bunton, you are with a group that sets standards for appraisers, is that correct?

Mr. BUNTON. Yes. That is correct.

Mr. LUETKEMEYER. I chaired this subcommittee a couple of years ago, and one of the things we were talking about at that time was a problem with appraisers, the certification of them from the standpoint, one of the criteria was that they had to have a college education, and I think they filled a 2-year apprenticeship after that. Is that still the case today, or have you changed that?

Mr. BUNTON. Effective May 1, 2018, that has been changed.

Mr. LUETKEMEYER. Okay. What did you change it to?

Mr. BUNTON. For the certified residential, it was a 4-year degree. Now, it is an associate's degree instead of a bachelor's degree, and it also—there are alternate pathways where you can take 10 college credits that would be equivalent to an associate's degree. As far as the experience, it has now been cut to 1,500 hours over 12 months. It was 2,000 hours over 24 before.

Mr. LUETKEMEYER. Because when you have a shortage of appraisers, I live in rural Missouri, a very rural town, 336 people, so we don't even have appraisers in our county, and so it is very difficult to find somebody. You have to go outside the county to find an appraiser. And my appraiser friends were telling me, hey, this threshold of a college degree and 2 years apprenticeship was killing them, not being able to get new appraisers into the business to then be able to go do these appraisals. So, thank you for doing that.

With regards to an appraisal itself, we have been discussing a little bit here about appraisals, but I think we need to remember that an appraisal is just a snapshot in time as to what the value of the property is today. My youngest daughter lives in Denver, which if you are an appraiser, you know the values out there just explode every day. She and her husband bought this house 5 years ago. They sold it recently for 60 percent more than they paid for it. During the crash of 2008, in Denver, the prices never went down. But in places like Georgia, those prices crashed, because they wound up losing 90 banks because of the value of the real estate.

I can go on and on in my own district. We had an area that crashed because of what happened with the markets. And it is not necessarily the neighborhoods; it was the fact that whether you wound up with inability to buy homes because you didn't have a job, whether it was new schools, new roads, losing factories, losing jobs. All of these things have an effect on the value of the property. And for all of you to try and sort through all this is quite an ordeal.

So, having been in the financial services industry for 40 years, I am familiar with a snapshot in time what that thing is worth, which brings me to the question, I guess, with regards to thresholds.

I know you are all unhappy about the threshold increase, but I am just kind of curious. Have you done any studies to see once what the loss ratio—how much it would increase by going from $250,000 to $400,000? Has anybody done a study on that? Nobody has done a study on it? Are you all against raising it from $250,000 to $400,000? Raise your hand if you are against it? Anybody neutral on it? Okay. So, if you are against it, tell me why if you are against it, if you can't prove your point.

Mr. WAGNER. You know, at the outset, I would say, Congressman, that it is an indication of a degradation in risk management in general. It signals a degradation in that vein, and do we know—

Mr. LUETKEMEYER. When was the $250,000 set in law or as a rule or suggestion?

Mr. BUNTON. In 1994.

Mr. LUETKEMEYER. So, 1994. What kind of inflation amount have we experienced from 1994 to 2019? At least double? At least 50, 100 percent?

Mr. BUNTON. I guess it is probably in the low 400s.

Mr. LUETKEMEYER. Okay. So, if you put an inflation multiplier on $250,000, where would you come up to, then, if you raised your threshold to match what it was in 1994? $400,000?

Mr. WAGNER. Somewhere in that range, but I think it is important to keep in mind what Mr. Bunton was pointing out earlier with the median price of a home. It is nowhere near that level. So, there were a whole lot of loans out there—

Mr. LUETKEMEYER. I can tell you from being a regulator in a previous life as well, when you go into a bank and you look at their mortgage loan portfolio, you don't look at every loan. You have what they call a cut, and you take a certain level, and all the loans above that, which are the big loans, which are the ones that if you lost it, you lost a lot of money. With little loans below that, while there is exposure there, because they are small and because if you lost one, yes, you would lose a little bit of money. But compared to losing a big one, if you cut at $40,000 versus $400,000, that is a big deal. I think for perspective point of view here, I am not for or against it at this point, I am just trying to discuss it, but I think we have to keep in mind the values, the inflation factor, the area of the country that we are in, and the fact that if you look in the large sense of a portfolio, is that really a risk to the entire portfolio?

Thank you, Mr. Chairman.

Chairman CLAY. I thank my friend from Missouri, and his time has expired.

The gentlewoman from Michigan, Ms. Tlaib, is recognized for 5 minutes.

Ms. TLAIB. Thank you, Mr. Chairman.

Thank you all so much for being here. We have a home ownership crisis in my district and across Michigan. We have lost more black home ownership than any other State in the country, in part because traditional mortgages are so difficult for people in my district to acquire.

Take Detroit as an example. In 2007, when my black neighbors made up 82 percent of the population, they received about 75 percent of Detroit home loans. By 2017, black Detroiters, despite still being 79 percent of the population, received just about 48 percent of home loans. When people can't get mortgages, they are forced to turn to land contracts, which I am working on to address, to realize their American Dream. And while land contracts can provide an important path to home ownership, due to the lack of oversight, too many in our community are being taken advantage of, and many are scamming folks out of their money in labor.

This situation has all been created in part by flaws in the appraisal process. Appraisals are lagging behind in sale prices, meaning folks are unable to get mortgages large enough to complete the deals and face a hurdle to the security and stability home ownership provides. Lagging appraisals put moving into many of our vacant homes and renovating them out of reach and perpetuates neighborhood decline.

This question is for Mr. Bunton. One of the things—when investors renovate the homes in Detroit and some of my Wayne County communities I represent, ultimately, it drives some of the property values up. Can original lower sale prices still be used as comparables for neighboring appraisals?

Mr. BUNTON. I am going to defer to the appraiser members on the panel. That doesn't sound correct, but I would defer to the appraiser members.

Mr. WAGNER. I am just going to say, and I think the gentleman earlier was talking about the comparable sales that get used. At the end of the day, based on sales, say, in a sales comparison approach, the value is the value, okay? Market value basically means, if you stick a sign in the yard, what will the property sell for? And if the market data in the area indicates a particular value, then it is what it is. And that is why, earlier, while I am very empathetic to this situation that you are referencing, it is bigger than the realm of appraisal. It involves lending and so forth, and I mentioned earlier that—

Ms. TLAIB. And I mention that a lot. Can you talk in detail, because what I have read and researched on is about how appraisal management companies perpetuate pressures from lenders to appraise a home at a cost different from the home's worth? With your membership in the appraisal community, are you all getting pressure to appraise at a higher cost?

Mr. WAGNER. There are times when we see pressure, and some of it is less than overt. There can be times when appraisers are actually supporting adjustments or attempting to support adjustments, and they are being questioned, second-guessed on their support and even for positive things, all right.

As far as actual pressure for hitting a certain number, that's not quite as prevalent, I think, as it once was. But, nevertheless, there are other kinds of pressures that appraisers experience with unreasonable turnaround times and so forth.

Ms. TLAIB. Thank you, Mr. Wagner. I appreciate it.

Mr. Perry, you were very thoughtful. I could take you home to my district, and everyone would be nodding their head. I have the third poorest congressional district in the country, and I always tell people: If you want to see what doing nothing looks like in communities of color, I will show you, and we end up paying as Americans twofold in trying to address poverty.

Land contracts are a huge struggle right now in my district. Many turn to land contracts. How can we make land contracts safer for home buyers? I am just curious about your opinion.

Mr. PERRY. I don't have an opinion on land contracts. I will say this, that there needs to be a lot of support for home buyers and sellers, that our devaluation report clearly identified areas where someone who is renting can actually buy a home.

Ms. TLAIB. That is right.

Mr. PERRY. We need to prioritize people living in districts where there is severe devaluation, provide them first-time home buyer assistance beyond what is given currently and give them the ability to buy a home, particularly in places like Detroit, because the conversation now is how to bring the middle class back in Detroit. You know, we should not bring in people to buy in Detroit at the expense of poor people because folks just don't go away. They move to other areas. So, there is an opportunity here.

Ms. TLAIB. Thank you, Mr. Chairman.

I yield back.

Chairman CLAY. You are welcome, and the gentlewoman's time has expired.

The gentleman from New York, Mr. Zeldin, is recognized for 5 minutes.

Mr. ZELDIN. Thank you, Mr. Chairman.

Thank you to the whole panel for being here today.

Ensuring that our consumers have accurate, transparent, and fair appraisal data is a critical priority in my district on Long Island and nationwide. That applies to potential home buyers or sellers or the professionals in the real estate industry. We definitely need more innovative ways to do this, and the rules and regulations need to be consistent and clear, but one thing that would not be helpful is several different sets of rules that could hurt the market, and most importantly, the consumers.

A question first for Ms. Trice. Are the appraisal rules and regulations for mortgages under the GSEs like Fannie and Freddie the same for FHA mortgages?

Ms. TRICE. No, they are not.

Mr. ZELDIN. Is it good policy to have a separate set of rules for FHA mortgages versus mortgages that are securitized by Fannie and Freddie or for other totally private mortgages?

Ms. TRICE. I think consistency and a clear roadmap is how you get credible appraisal reports and reliable information.

Mr. ZELDIN. How much influence do the GSEs—Fannie Mae and Freddie Mac—exert over the appraisal process today?

Ms. TRICE. They virtually own it. They are the de facto regulator, if you will. They create the forms that the entire industry uses. The VA and the FHA use the Fannie and Freddie-devised form that is under development now for a new form, and there is even pressure being put upon the VA—I think there is some proposed regulation that the VA is being asked to use unlicensed individuals to inspect properties because that fits the mold that the GSEs are going towards.

Mr. ZELDIN. Do the GSEs consistently require the use of appraisals on the loans they purchase?

Ms. TRICE. I'm sorry, say it one more time?

Mr. ZELDIN. Do the GSEs consistently require the use of appraisals?

Ms. TRICE. No. They have a waiver program where there is a reps and warrants relief to the lender. Both entities have different programs, and today, they are piloting a hybrid appraisal report where the inspection is being done by unlicensed individuals. Literally, there are no qualifications. You could be an Uber driver today and show up to inspect a home tomorrow. That will be input into the appraisal process.

Mr. ZELDIN. I appreciate that. I am actually going to yield the remainder of my time to Mr. Duffy.

Mr. DUFFY. I appreciate the gentleman for yielding.

I just want to note that I thought it was a good point to make that appraisers don't make markets; they reflect the pricing in the market. I don't think we can lose sight of that.

But, also, Mr. Perry, you made me think a lot, and I appreciate your testimony. I don't want you to take this out of context. I am trying to see, what is causing the problem? What are the solutions to problems? But we have had a lot of conversations in this room about affordability. And what happens to communities if we say, "You know what, the market says," as someone puts a sign in their yard and they get an offer on it, "the home is worth this much, you know," supply and demand, and buyers and sellers come together at a meeting of the minds; if we bring those prices up 23 percent, what happens to the affordability of those homes in the neighborhood in which we are talking about? It probably makes it less affordable, right?

Mr. PERRY. That is why I said this is about providing support on the supply and the demand, that people, one, have to receive—it could be anything from a tax credit to make up for differences to also additional loan support, but clearly, there is market failure. I would differ in the sense of the market is the market.

Mr. DUFFY. But we get in trouble—if we give people mortgages on houses they can't afford, and they can't pay for them, and then, all of a sudden, we have done something wrong about giving mortgages that they can't pay for. I look at it, as the prices have gone up, I don't think there is any racial overlay of what has happened at The Wharf or the Navy Yard down here, but prices have gone up dramatically. People who own the properties, they made a lot of money. But what has happened with—I don't know anyone on this panel who can buy a place down there. What has happened? There is a gentrification problem that has gone on too, and you have all of a sudden moved people out of one area.

Mr. PERRY. I just want to emphasize, the type of devaluation we are seeing is—you have to assume that there is something systemic. And the market is failing if you have communities where you have 50 percent comparable homes priced 50 percent or more or less than that same home a few blocks away. So what I am getting at is there has to be some effort to say: Hey, assessors, lenders, we have to recalibrate this.

Mr. DUFFY. I know my time is up, but I would like to work with you more on this. I want to understand your study a little further. I would imagine, though, that if an offer comes in 50 percent or 25 percent higher, and the appraiser is appraising it at 25 percent less, and so he can't get a mortgage on the property, now, that would be a problem.

But if we are having a meeting of the minds where the buyers and sellers are meeting and the appraisal comes in where the buyers and sellers have matched on price, I would see that as less of a problem. I would like to talk to you more if you are willing and kind of drive into this because I am picking up what you are putting down and I think we should engage further.

Chairman CLAY. At this point—no, no. We are going to enter into a second phase. We are going to call it a lightning round where each Member is limited to 2 minutes.

Mr. DUFFY. Mr. Chairman, we make up the rules as we go, right?

Chairman CLAY. That is right. It is 2 minutes, but it will be equal time. And so let me start by saying that, Mr. Perry, I appreciate the fact that you have highlighted the disparities in the process of appraisals, and I would urge the rest of the panel, in order to address the wealth gap, the racial wealth gap, that we think outside of the box, that we actually look at other methods than comparable sales in the appraisal process if there is a geographic area that you are not getting the market value of the homes. Look at the cost of replacement of the home. We can think outside the box, and we can come up with solutions as far as how many or how we allow others to enter this profession as apprentices, how we increase diversity in that area.

And so, Mr. Dickstein, perhaps you can tell us, how could we do this in a method that is outside of the traditional box that you now operate in?

Mr. DICKSTEIN. We currently have three methods as appraisers that are acceptable: first, we have one you alluded to, the sales comparison; second, we have the cost approach; and third, we have the income approach. So appraisers do have the ability to look at a cost approach, looking at the value of the land, a new structure. We have the ability to look at rents in the area and determine value based on rents. But like whatwas said earlier, I think it is the chicken or the egg. You have so many lenders, investors, servicers who, as soon as the loan goes into a default situation, they are now left with—I think Mr. Perry alluded to maintenance of the home. A lot of these people in some of these areas just can't afford to maintain the home properly. So now that passes on to a lender and investor, and now they have an asset that they are holding onto that is in disrepair. They now have holding costs in the form of property taxes, upkeep in the neighborhood, property preservation. Now, they want this asset off their book so they throw it on the market priced for a quick sale.

Chairman CLAY. At a discount.

Mr. DICKSTEIN. At a discounted price. So what happens is sometimes if you get a market that is going through a downturn, whether it be job loss in the area, loss of manufacturing, loss of any type of income stability for that neighborhood, there is a trickle down, and it affects the neighborhood as a whole.

Chairman CLAY. It is cyclical.

Mr. DICKSTEIN. Absolutely. And appraisers are just reporting what is happening.

Chairman CLAY. All right. And I appreciate that.

And now, Mr. Zeldin, would you like to—

Mr. ZELDIN. I would like to yield my 2 minutes to Mr. Duffy.

Mr. DUFFY. Thank you.

Chairman CLAY. Go right ahead.

Mr. DUFFY. Can I just ask, what should our takeaways be from this hearing? Give us the snapshot of the top lines of what Mr. Clay and I and this subcommittee should be working on as we leave today. Mr. Bunton, we will start with you.

Mr. BUNTON. The first one is, let's use valuation professionals to determine the value of the collateral for loans, and more and more, we are getting away from that, whether it is ABM or non-appraisers.

Mr. DUFFY. You like human beings.

Mr. BUNTON. Pardon me?

Mr. DUFFY. You like human beings.

Mr. BUNTON. Correct.

Mr. DUFFY. All right. Mr. Wagner?

Mr. BUNTON. With technological tools. Absolutely.

Mr. WAGNER. I would like to emphasize the use of human beings as well, and I would also like to emphasize one other thing relative to thinking outside the box, so to speak. I tried to touch on it earlier, and that is some of the programs that are under development in Detroit and St. Louis, and it involves lending and how a loan is structured.

And, also, in terms of promoting diversity within the industry, just as an example, the Appraisal Institute has a number of ongoing—

Mr. DUFFY. You have to go quickly, Mr. Wagner. I have three more witnesses to get to. What is my takeaway?

Mr. WAGNER. That we are promoting diversity as well.

Mr. DUFFY. Okay. Mr. Dickstein?

Mr. DICKSTEIN. I echo the sentiments of both Mr. Bunton and Mr. Wagner.

Mr. DUFFY. Human beings.

Mr. Perry?

Mr. PERRY. I am going to emphasize data. It is clear that human beings have burdened some and not advantaged others, that the decisions that are made at the appraisal process have to be countered with data in the report that I authored.

Mr. DUFFY. Ms. Trice?

Ms. TRICE. Appraisal reforms with a focus on safety and soundness so that we have a safe housing system for all Americans.

Mr. DUFFY. Thank you. Listen, I think you all have done a great job today giving us your feedback and viewpoint, very diverse, but I think very useful to us, and I appreciate your time and your testimony.

I yield back.

Chairman CLAY. Thank you so much.

And, Ms. Tlaib, we will let you finish it off.

Ms. TLAIB. I was getting into it with Mr. Perry. So, the one thing that I noticed is, I think I saw some statistics that a majority of my residents in the 13th Congressional District, close to half of them are renters now. We used to be, like, 70 percent home ownership. It created stability, even built up our school system. Everything is so connected to home ownership. The one area I kept looking at was the fact that they were paying 30 percent more in their income. So if I got them into a home, which sometimes some are worth, you know, outside of the 7.2 miles in downtown Detroit, in those areas, was able to—homes that are, like, valued at $40,000, $50,000, but people are not lending at those kinds of low prices, is them not being able to get access to that. But even when they came out to appraise in one neighborhood specifically, it came out even lower than that, and then they would have to come up with the cash difference.

And all of the appraisals—all of you folks are obviously working in a broken system, but I also ask all of you, and Mr. Perry, maybe you can help in creating this, that I don't think everything fits into just one little box and that we are looking at all of the circumstances, all of the things. Even projecting out what is happening now in the 7.2 miles, how that is going to trickle down into the other neighborhoods. I have to tell you what I am seeing is that there are neighborhoods, honestly, where the houses look the same. It is the exact same house, exact same issues, high rates of this or that way. But because more white people are moving into that neighborhood, the prices skyrocketed. I don't understand why.

And then there are some of my residents who obviously benefit from that because they are, like, you know, I am going to turn around and just sell it and go to the suburbs where it is cheaper to live because now the pricing is high, and they have to pay income tax in Detroit and all of those things.

Even my colleague on the other side of the aisle, trying to get down whether it is human or not, I just feel like, even with appraisals, we are just sticking to these, like, checklists of things. And I feel like if it is in a low- to moderate-income neighborhood, that you all need a little bit more flexibility in how you value a home with all of the—and, Mr. Perry, you know, every time—

I am a social worker at heart. I come from the nonprofit sector. I just know for 12 years that one of my residents—this is a true story—is paying $700 a month on rent, but I can get him into a house for $400 a month in a mortgage. I don't understand but for the fact that he can't, in the same neighborhood, get it to be appraised for what—it is, like, that difference is why he can't because he doesn't have the cash in hand. I just don't understand why the system is built that way.

Mr. PERRY. I just always remind people that we have been in this period before. After World War II, we enacted policies that enabled people to buy a home. We can create Federal policy that is creative, that is innovative to get black and brown people into homes. We keep trying to avoid the policy conversation to get people into homes and back into our sectors that are clearly biased. Again, it is not just appraisals. It is lending. It is real estate agents. It is the economic structure. There are a lot of things, but we all have a responsibility to have some legislation to address racism and structural bias. We have a responsibility to do that.

Chairman CLAY. Thank you. And on that note, as I close, thank you, Mr. Perry, and I thank the entire panel of witnesses for your contribution to this hearing today. I found it quite educational. And as I close, I will note the assistance of the Metropolitan St. Louis Equal Housing and Opportunity Council, and I look forward to their continued guidance in the area of appraisals.

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

This hearing is adjourned. Thank you.

[Whereupon, at 3:49 p.m., the hearing was adjourned.]

A P P E N D I X

June 20, 2019

Testimony of
David S. Bunton, President
The Appraisal Foundation

What's Your Home Worth? A Review of the Appraisal Industry

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

June 20, 2019

The Appraisal
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INTRODUCTION

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

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

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

Rather, the Foundation:

- is a non-profit 501(c)(3) educational organization;
- was founded by eight national appraisal organizations 32 years ago;
- sets standards of excellence, promotes education and upholds the public trust
- serves as an umbrella organization comprised of approximately 100 organizations and government agencies with an interest in valuation (Attachment 1);
- was created to foster professionalism in appraising;
- strives for excellence, consistency, unity and trust in the valuation profession.

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

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

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

OVERVIEW

This year marks the 30th anniversary of the adoption of the *Financial Institutions Reform, Recovery, and Enforcement Act* (FIRREA or Act) in which Congress ushered in groundbreaking reforms to ensure the safety and soundness of the federal financial deposits and heighten consumer protections. Title XI of FIRREA created the appraiser regulatory structure and required appraisers to meet qualifications and follow national uniform standards of practice set by The Appraisal Foundation (Foundation) and its Boards. At the time Title XI was adopted, the intent was that all mortgage transactions backed by the federal government came under the protections of the Act.

In the ensuing three decades, all U.S. jurisdictions set up appraiser licensing and enforcement agencies. They work to ensure that those who hold a real property appraiser credential are qualified and perform appraisals in accordance with professional standards. Currently, there are approximately 75,000 licensed and certified appraisers across the United States who are trained to competently and ethically perform appraisal assignments.

The qualification criteria to become an appraiser is more robust today with structured appraisal-specific education, practical experience, and a uniform, national examination in place to gauge minimum qualifications for those valuing the world's largest economy. Likewise, the *Uniform Standards of Professional Appraisal Practice* (USPAP) is viewed as the gold standard globally. USPAP has been successfully tested in our legal system by being the cornerstone of numerous regulatory and court decisions regarding valuation. Lenders and consumers have assurance that appraisals performed to the standards are fair, impartial, and objective, and completed without bias.

We applaud the recent bipartisan efforts of Congress to once again allow state licensed appraisers to perform appraisal assignments for Federal Housing Administration (FHA) loans. With similar bills pending in the House and Senate, we encourage your support for swift passage.

But, all is not well. The last thirty years were also witness to federal agencies doing their best to circumvent using these trained professionals. Likewise, the government sponsored enterprises are taking on riskier practices that leave appraisal protections on the sidelines. Through exemptions, appraisal waivers, promoting evaluations in lieu of appraisals, and encouraging lenders to use unlicensed individuals, the federal financial institutions regulatory agencies estimate that a mere 10 to 15 percent of all mortgage transactions backed by the federal government and U.S. taxpayers are currently subject to the protections Congress enacted through Title XI.

SPECIFIC TOPICS OF DISCUSSION REQUESTED BY THE SUBCOMMITTEE

The *De Minimus* Threshold and Federally Related Transactions

The *De Minimus* Threshold

In the summer of 1990, three years after the enactment of FIRREA, the federal financial regulatory agencies developed their appraisal regulations, including setting the *de minimus* threshold, below which real estate transactions would not have to be appraised by a state licensed or certified appraiser. The initial *de minimus* threshold was set by the agencies at $50,000, with the exception of the Federal Reserve Board, which set its threshold at $100,000.

In June of 1994, the federal financial regulatory agencies increased the *de minimus* to $250,000 for residential real estate transactions. Currently, there is a pending proposal to increase the *de minimus* once again to $400,000.

We strongly oppose an increase because it would further dilute the intent of Title XI of FIRREA. We are far from alone in this belief. The overwhelming majority of comment letters received by the agencies about the proposal were in opposition to the increase, and several commenters requested the agencies to hold a hearing on this topic. Unfortunately, the agencies declined to hold such a hearing. Title XI was put in place to ensure the safety and soundness of our deposit insurance fund. The value of the underlying collateral in a lending transaction needs to be determined by a professionally trained appraiser who adheres to performance standards and is credentialed by a state.

The impact of such an increase is enormous. The median existing-home price for all housing types in April was $267,300, according to the most recent report from the National Association of Realtors. A $400,000 *de minimus* would exempt most residential mortgage transactions. An individual's primary residence is often their single largest investment and neither lenders nor borrowers would be afforded the protection of having a trained professional determine whether an appropriate price is being paid for a property.

As stated above, when a loan amount is below the established *de minimus* threshold, financial institutions are not required to obtain an appraisal. In these transactions, lenders utilize alternatives to appraisals, which they call ***evaluations***. Evaluations have many similarities to appraisals, but there are some differences with respect to development and reporting (Attachment 2). In addition, there are some key distinctions between appraisals and evaluations. First, there are no codified requirements addressing the development and reporting for evaluations. The federal financial institutions have developed guidance[1], but a recent ruling underscored that such guidance is simply that, and is not enforceable.[2]

There are also no codified qualification requirements for individuals providing evaluations. The guidance does include some very generic references about qualifications, saying the individual *should* have appropriate education and experience to perform the evaluation. However, as stated above, this guidance is not binding and is unenforceable.

Because the guidance on evaluations does not require an individual to possess a credential of any type, there is no public accountability similar to what exists for individuals performing appraisals. If someone performing an evaluation failed to do so ethically and competently, there is nothing that would hold the individual responsible for such actions.

Recommendations:

- **Set parameters for the agencies to abide by when setting the threshold amount.**
  - Set a cap on the threshold amount that is well *below* the median home sales price.
  - Restrict the use of the threshold exemption to transactions where the loan to value ratio is less than 70 percent.
  - Require that the threshold exemption may only be used when the lender is going to hold the note for the term of the loan.

- **Codify requirements for the agencies' use of evaluations**
  - If lenders continue to utilize alternatives to appraisals (i.e., evaluations), require the use of credentialed appraisers in these transactions.
  - Require evaluations to be performed in compliance with USPAP.

Federally Related Transactions

Related to the *de minimus* is the issue of what constitutes a federally related transaction. When Congress passed FIRREA, the intent was that most residential mortgage transactions would be considered federally related transactions and thus come under the protections established by the Act.

In the early 1990s, the federal financial regulatory agencies adopted a series of regulations that resulted in 13 instances where a transaction is no longer considered a federally related transaction (Attachment 3). These "carve outs" greatly reduced the

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[1] *Interagency Appraisal and Evaluation Guidelines*, December 2010
[2] *Interagency Statement Clarifying the Role of Supervisory Guidance*, September 2018

number of federally related transactions. Staff of these agencies have estimated that fewer than 15 percent of residential mortgage transactions come under the current definition of federally related transactions.

The agencies recently made their position clear that transactions coming under the term were limited. In a May 17, 2017 letter to the Association of Appraiser Regulatory Officials (AARO), they outlined the numerous exemptions to transactions that come under the definition (Attachment 4). Individuals involved in the appraiser regulatory system were alarmed to learn that they were operating under the false impression that the majority of residential mortgage transactions are federally related.

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

Recommendations:

- **Clarify the definition of "federally related transaction" to include all residential mortgage transactions that are backed by the federal government and thus American taxpayer.** While it seemed reasonable to give the agencies the ability to exempt certain transactions, the decimation of the term by agency regulation is clearly an abuse of power and disregards the Congressional intent of FIRREA.

- **Require all transactions involving Government Sponsored Enterprises (GSEs) to utilize state licensed or certified appraisers, and require USPAP-compliant appraisals for those transactions.** Because the GSEs are not statutorily mandated to use state credentialed appraisers or comply with USPAP, the lack of a legislative mandate could allow them to change their policies overnight.

Appraiser Independence

The Dodd-Frank Act took some steps to strengthen appraiser independence[3]; however, there is much more that can be done.

Many appraisers can relate experiences from years past of being pressured by lenders to "make the deal" or run the risk of not being compensated or being removed from an "approved appraiser list," prohibiting the appraiser from performing future appraisals for that lender. Appraisers are required to be independent, impartial, and objective, and such antics were obviously met with great disdain. Therefore, upon learning that federal legislation would address appraiser independence, many appraisers felt hopeful that they would be able to practice ethically without facing such intimidation.

[3] Dodd-Frank Wall Street Reform and Consumer Protection Act (2010), revisions to 12 U.S.C. 1639e, 12 U.S.C. 3351, 12 U.S.C. 3353.

While Dodd-Frank included prohibitions against such behavior, it also resulted in a proliferation of Appraisal Management Companies (AMCs). AMCs are companies through which mortgage lenders contract for appraisals, and they are designed to act as a firewall between lenders and appraisers. Conceptually, appraisers were not necessarily opposed to the AMC model, as they foresaw an intermediary that might protect them from lender pressures experienced in the past. However, when appraisers realized that AMCs would be funded by taking a portion of the *appraiser's* fee, the entire system felt the shockwaves. Appraisers who had a track record of performing ethically and competently for many years were now asking, ***"Why do I have to sacrifice my income to avoid facing pressure and intimidation?"***

In addition, borrowers (who pay the appraisal fee when applying for a mortgage) typically have no idea that an AMC is involved in the transaction. A borrower paying a $400 appraisal fee, for example, assumes the appraiser receives that amount. However, the borrower is completely unaware that the AMC receives a share (sometimes a significant one) of that fee. This scenario can also be confusing to a borrower if an appraiser is required to comply with any AMC-specific requirements not imposed by the lender. If the borrower has questions about the appraisal and contacts the lender, the lender might not be able to fully explain why an appraisal was performed in the manner it was.

Another key aspect appearing to fall short of Congressional intent is *enforcement* of appraiser independence requirements. While Dodd-Frank required the creation of an "Appraisal Complaint National Hotline" by the Appraisal Subcommittee[4], the hotline does not track complaints to determine whether alleged violations of appraiser independence actually occurred, whether action was taken, or whether an entity committing such violations revised its policies to avoid future violations. The hotline created provides some valuable information on where complaints can be filed, but without a process to track such complaints through resolution, it is not possible to tell whether any remediation or improvement has occurred. An unscrupulous lender that may not believe change is needed due to lax enforcement could very well continue to operate in that manner. The cumulative effect may result in appraisers feeling pressured or intimidated, causing them to leave the profession and reduce the number of appraisers available to provide valuation services.

Recommendations:

- **Require AMC fees to be paid by the lender** – Lenders are not required to use AMCs. Lenders may satisfy appraiser independence requirements by establishing an internal firewall within their institutions. Lenders wishing to "outsource" this function to AMCs should bear the burden of this cost, not pass it on to the appraiser. In the past, lenders paid the full fee to appraisers.

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[4] Dodd-Frank Wall Street Reform & Consumer Protection Act (2010), revisions to 12 U.S.C. 3351

- **Require AMC fees to be identified separately in closing documents –** Borrowers paying an "appraisal" fee should have the right to know exactly where that fee goes.

- **Require mandatory tracking and reporting related to complaints of violations of appraiser independence** – To accurately gauge the effectiveness of appraiser independence requirements, it is necessary to evaluate complaints to determine if violations occurred, and what steps were taken to remediate such actions.

The Impact of Technology on the Appraisal Profession

Technological advances in the appraisal profession offer the opportunity to streamline the valuation process and make it more efficient and less costly. However, these new technology programs have their limitations, and we should never lose sight of the fact that accurate appraisals are the basis of the public's trust in the valuation profession.

Recognizing the role of professional appraisals in promoting the public trust, Congress passed Title XI of FIRREA in 1989. It tasked The Appraisal Foundation with the creation of appraiser qualifications and standards that are designed to lead to independent and reliable appraisals performed according to ethical guidelines.

Since the passage of Title XI, we have seen the advent of "big data" and evolving technology, and the introduction of Alternative Valuation Products, including Automated Valuation Models (AVMs). Some individuals believe a computer can provide an equally "accurate" opinion of value to appraisers. As these technologies become more refined, it's likely that, in certain cases, that may be true.

In areas with extremely homogenous housing and ample sources of market data, a well-written AVM may be an appropriate way to analyze the collateral on a relatively low-risk loan. Estimates of real property value can be determined by computer, taking into account the number of bedrooms and bathrooms in a home, square footage, property size, and other objective factors.

However, there are many markets consisting of properties with varying ages, construction quality, condition, renovation levels, lot sizes, view amenities, etc.—not to mention special financing arrangements or seller concessions. It is in these markets where a professional appraiser is needed to apply the type of judgment that a computer cannot replicate. While a computer can do a great job of "crunching" numbers, its output is only as good as its input. If the information required to properly analyze market activity is not entered by a trained professional with a solid understanding of the marketplace, the ensuing results may be suspect. (See Attachment 5, "Why Appraisers Matter")

In summary, human appraisers, working with the tools of technology, are needed to determine the overall appeal and market value of a property. The consequences of an inaccurate or incomplete appraisal are significant and can impact the purchaser, as well as, in the case of federally backed mortgages, the federal government and the taxpayer. Paying a purchase price that exceeds the value of a property based on an inflated appraisal can cost consumers thousands of dollars and potentially lead to a default.

Despite our concerns, we recognize that technology has its place in the future of the valuation profession and we embrace it when it doesn't compromise public trust. For example, Dodd-Frank directed federal regulators in 2010 to work with The Appraisal Subcommittee and the Foundation to develop standards for AVMs[5]. Nine years later, regulators have not reached out to the Foundation to do this work; however, we are anxious to be helpful in this regard.

Technology has allowed Fannie Mae and Freddie Mac to aggregate the data appraisers have produced for their mortgage loans over many years, resulting in one of the most significant databases ever created related to residential real estate. Sharing that data with appraisers would give them more information and enable them to develop an accurate appraisal more quickly and efficiently.

The Foundation is using technology to address a lack of certified appraisers willing to supervise trainees in rural areas. Congress shares the belief that we need to recruit more appraisers to alleviate long delays in many regions of the country. As a result, we are creating the Practical Applications of Real Estate Appraisal (PAREA) program to help alleviate the problem many trainees have experienced, where they have been unable to find supervisors to oversee their practical experience requirements. This program uses technology to provide practical experience in a simulated environment. PAREA is in the early stages of development and we hope to identify a dedicated funding source to bring it to market.

We look forward to working with Congress, our regulators, stakeholders, and the appraisal profession to take full advantage of technology in a way that advances the industry and promotes the public trust.

Recommendations:

- **Contact the Federal financial institution regulatory agencies to seek an explanation for the nine-year delay in establishing quality control standards for AVMs and a timeline for the completion of the draft standards.**

- **Direct the Federal Housing Financing Authority (FHFA), the overseer of Fannie Mae and Freddie Mac, to make their residential databases available to appraisers in good standing, incorporating all the necessary privacy safeguards.** Appraisers collectively supply the data to these databases and it is critical to give them access.

[5] Dodd-Frank Wall Street Reform & Consumer Protection Act (2010), revisions to 12 U.S.C. §3354

Diversity in the Appraisal Profession

Diversity within the appraisal profession does not reflect the racial composition of the U.S. proportionately. A recent survey conducted by The Appraisal Foundation found that 73 percent of respondents identified as male while 23 percent identified as female. 90 percent identified as Caucasian, 4 percent identified as Hispanic or Latino, 2 percent identified as Black or African American, and 1 percent identified as Asian. The findings of this survey were similar to other surveys conducted by various appraisal organizations.

The Foundation realizes there is much to be done to increase diversity in the profession. We are committed to working with our affiliated organizations to ensure that the appraisal profession reflects the broad diversity of consumers reliant on valuation services.

The Foundation is pleased to report increased gender diversity on our Board of Trustees (BOT) and our two independent boards, the Appraiser Qualifications Board (AQB) and the Appraisal Standards Board (ASB). For the first time in the 32-year history of the Foundation, the ASB is majority female. The BOT is 33 percent female. Both of these boards exceed the percentage of women in the appraisal profession.

The Foundation actively participated in International Women's Month in March by profiling our women leaders in industry trade publications and highlighting why a career in appraising is a good choice for women. The Foundation understands that when creating gender and racial diversity, it must be an intentional effort. The Foundation committed to greater gender diversity several years ago, and we are seeing the fruits of those efforts now.

Another Foundation project that may help to increase racial diversity within the appraisal profession is our Veterans Outreach Initiative. This past May, we developed a resource webpage that provides veterans with information about a career in appraising and a network of Appraisers who are veterans. Brad Swinney, U.S. Army Veteran and member of the AQB, recently noted, "We firmly believe that warriors who protected the greatest nation make for proud guardians of the public trust through valuation, which helps protect the greatest economy in the world." Since the page has launched, the response from appraisers who are veterans wanting serve on the network and veterans looking to speak with appraisers has surpassed our expectations.

Pew Research recently found that as the United States of America has become more racially and ethnically diverse, so too has the U.S. military. The research found that racial and ethnic minority groups made up 40 percent of Defense Department active-duty military in 2015; up from 25 percent in 1990. As the most racially and ethnically diverse class of veterans are returning home and transitioning to a new career, we want them to consider the benefits of becoming an appraiser.[6]

While our veterans' outreach activities will help reach a racially and ethnically diverse audience, we continue to explore additional avenues. The AQB established a review program for college degrees in real estate. Under this program, the AQB analyzes real estate-related degrees, at no cost to the school, to determine how the education required to obtain a degree can be applied to the *Required Core Curriculum* in the *Real Property Appraiser Qualification Criteria*. State appraiser regulatory agencies use this information when reviewing the educational qualifications of applicants that hold such degrees. To date, the AQB has analyzed 20 undergraduate and graduate programs. The AQB is working to expand its real estate degree review program to colleges with large student populations of veterans as well as to historically black colleges and universities.

The Foundation is also engaged in activities to reach first-time and low-income homebuyers. To help demystify the appraisal process, the Foundation created a homebuyer educational module titled, "What Every Homebuyer Should Know About an Appraisal." The Foundation developed this program to assist presenters of first-time homebuyer education classes around the country. It includes vital information and resources for consumers on what an appraisal entails, how an appraiser determines value, and how to interpret an appraisal report. This information and our other consumer resources should help homebuyers not fall victim to predatory lending schemes – schemes that disproportionally targeted racial and ethnic minorities during the years leading up to the financial crash in 2008. We are pleased that these modules are being used by national affordable housing organizations.

Much of these efforts are due to our long-standing relationship with the National Society of Real Estate Appraisers (NSREA), the largest trade organization representing African American real estate appraisers. NSREA is a member of The Appraisal Foundation Advisory Council (TAFAC). TAFAC member organizations represent various professions and occupations with an interest in valuation including appraisers, home builders, real estate brokers, financial institution regulators, federal land acquisition agencies, the secondary mortgage market, and the private mortgage insurance industry.

While these programs have seen some successes, the valuation profession must do more to increase diversity among appraisers. **The Foundation is committed to working jointly with the professional appraisal organizations to continue efforts to increase minority participation in the valuation profession and to enhance protections for minority homebuyers, and to identify more ways to achieve those goals.**

[6] Parker, K, Cilliuffo, A., & Stepler, R., (2017, April 13) 6 Facts about the U.S. military and its changing demographics. Pew Research Center, Fact Tank. Retrieved June 17, 2019 from https://www.pewresearch.org/fact-tank/2017/04/13/6-facts-about-the-u-s-military-and-its-changing-demographics/

Performing Appraisals without Bias

To comply with the *Uniform Standards of Professional Appraisal Practice* (USPAP), appraisers are required to be independent, impartial, and objective, and to perform assignments without bias. An appraiser failing to comply with these basic tenets of fairness and equality would be in violation of the ETHICS RULE in USPAP, which is the most significant breach an appraiser could commit. Such a violation would likely result in the revocation or required surrender of an appraiser's credential.

Due to the importance of this issue, the Appraisal Standards Board (ASB) of The Appraisal Foundation has developed strict prohibitions in USPAP to which appraisers must adhere. The ASB has also developed guidance designed to ensure appraisers understand how to comply with these fundamental obligations. Addressing this point, the Conduct section of the ETHICS RULE in USPAP states:

> ***An appraiser must not use or rely on unsupported conclusions relating to characteristics such as race, color, religion, national origin, gender, marital status, familial status, age, receipt of public assistance income, handicap, or an unsupported conclusion that homogeneity of such characteristics is necessary to maximize value.***

To ensure appraisers clearly understand this prohibition, the ASB published Advisory Opinion 16, *Fair Housing Laws and Appraisal Report Content*. This guidance, which can be found in the USPAP publication, states, in part:

> ***Fair housing law(s) preclude the use of certain specific information or supported conclusions related to protected group(s) in some assignments. Accordingly, an appraiser should be knowledgeable about the laws that affect the subject property of an assignment. Laws and regulations on fair lending and fair housing (such as the Fair Housing Act; the Equal Credit Opportunity Act (ECOA), and the laws and regulations of applicable federal, state, and local jurisdictions) continue to evolve. Further, appraisers must continue to provide appraisals that do not illegally discriminate or contribute to illegal discrimination.***

Thus, appraisers complying with USPAP do **not** produce unfair or discriminatory valuations.

In some cases, when an appraiser's opinion of value is questioned, there are some who mistakenly believe the appraiser "sets the value" for the property. However, this could not be further from the truth. When providing opinions of *market value*, the very premise is that the appraiser is simply *reflecting* the actions in the marketplace, not determining them. An excerpt of the definition of *market value* used by federally regulated financial institutions specifically requires the appraiser to recognize actions in the marketplace:

"The most probable price which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus."

Further characteristics of that definition underscore that the appraiser's opinion of market value is to be based exclusively on the actions of the marketplace:

- *Buyer and seller are typically motivated*
- *Both parties are well informed or well advised, and acting in what they consider their own best interests*
- *A reasonable time is allowed for exposure in the open market*
- *The price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale*

With respect to Fair Housing, USPAP Advisory Opinion 16 recognizes an appraiser's obligation to accurately reflect the actions of the marketplace, and cautions the appraiser:

> ***An appraiser should research the actions of participants in the subject's market to identify factors having a direct favorable or unfavorable influence on marketability or value. Failure to extract pertinent market information (e.g., sales, rents, occupancy rates, expense ratios, capitalization or discount rates, construction costs, depreciation, or exposure times) from the subject's market could produce conclusions that are misleading and/or illegally discriminatory.***

Therefore, appraisers are required to base their analyses, opinions, and conclusions on the actions of the marketplace, and are prohibited from developing conclusions that could be discriminatory.

Recommendation:

- **Require compliance with USPAP** – As stated previously, appraisers complying with USPAP do <u>not</u> produce unfair valuations. However, there are some who are advocating that not all valuation assignments need to be performed in compliance with USPAP. Allowing valuations to occur without the obligations for ethical and competent practice set forth in the battle-tested USPAP standards creates a possibility for unfair or discriminatory valuations.

CONCLUSION

As we observe the 30th anniversary of Title XI, there is much to celebrate. The Act created a regulatory system designed to ensure that real estate appraisals are conducted in a way that is fair, objective, impartial and ethical. It helps protect the integrity of the deposit insurance system and promote public trust in real estate appraisals. Over the decades, it has advanced professionalism through robust education, training and testing. The real estate appraisal profession is stronger than ever, and this has been achieved without the use of appropriated funds.

However, as we have outlined in this testimony, the intent of the law has not been fully realized. Congress' intent and the law's potential have been circumvented by regulatory exemptions, waivers and other actions that have kept a majority of residential real estate transactions outside of its protections. Our testimony includes recommendations on how we propose to correct this.

The Appraisal Foundation appreciates the opportunity to share our perspectives with you today and we urge this Subcommittee and all members of Congress to continue to use the Foundation as a resource on valuation-related matters.

The Appraisal Foundation

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

The Appraisal Foundation Advisory Council:

ORGANIZATIONS OF APPRAISERS

American Society of Appraisers *
American Society of Farm Managers and Rural Appraisers *
Appraisers Association of America *
Association of Independent Mortgage Experts
Association of Machinery and Equipment Appraisers
Association of Texas Appraisers
Canadian National Association of Real Estate Appraisers
Columbia Society of Real Estate Appraisers *
Equipment Appraisers Association of North America
Illinois Coalition of Appraiser Professionals
Instituto de Evaluadores de Puerto Rico *
International Association of Assessing Officers *
International Right of Way Association *
International Society of Appraisers *
Maryland Association of Appraisers
Massachusetts Board of Real Estate Appraisers *
Midwest Appraisers Association
National Association of Appraisers
National Society of Real Estate Appraisers
North Carolina Professional Appraisers Coalition *
North Carolina Real Estate Appraiser Association
Ohio Coalition of Appraiser Professionals
Real Estate Valuation Advocacy Association
Royal Institution of Chartered Surveyors
South Carolina Professional Appraisers Coalition *
Virginia Coalition of Appraiser Professionals
West Virginia Council of Appraiser Professionals

USERS OF APPRAISALS

American Bankers Association *
American Institute of Certified Public Accountants
Conference of State Bank Supervisors
Counselors of Real Estate
Farm Credit Council *
Federal Agricultural Mortgage Corporation
Institute for Professionals in Taxation
Mortgage Bankers Association
National Association of Federal Credit Unions
National Association of Home Builders
National Association of Mortgage Brokers
National Association of Realtors *
National Auctioneers Association
National Council of Real Estate Investment Fiduciaries
Relocation Appraisers & Consultants
Worldwide ERC

GOVERNMENT AGENCIES AND ORGANIZATIONS

Association of Appraiser Regulatory Officials
Fannie Mae
Federal Highway Administration
Federal Transit Administration
Freddie Mac
General Services Administration
Internal Revenue Services
US Department of Agriculture, Farm Service Agency
US Department of Agriculture, Forest Service
US Department of Agriculture, Natural Resources Conservation Service
US Department of Agriculture, Rural Development
US Department of Energy, Bonneville Power Administration
US Department of Housing and Urban Development
US Department of Justice
US Department of the Army
US Department of the Interior, the Office of Valuation Services
US Department of the Navy
US Department of Veteran Affairs

**Also a Sponsoring Organization of The Appraisal Foundation*
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The Appraisal Foundation

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

The Appraisal Foundation Industry Advisory Council:

FOR-PROFIT ORGANIZATIONS

Allstate Appraisal
Amrock
AVMetrics
Bank of America
BBG
CBRE
Clarocity Corporation
Cushman & Wakefield
CoreLogic|FNC, Inc.
First American Mortgage Solutions, LLC
Genworth Mortgage Insurance Corporation
HouseCanary
JPMorgan Chase
JLL Valuation & Advisory, LLC
Lowery Property Advisors
LW Hospitality Advisors
Miller Samuel, Inc.
Morgan Stanley Mortgage Capital
Mortgage Information Services
National Association of Jewelry Appraisers
Newmark Knight Frank Valuation & Advisory
OnCourse Learning
PCV Murcor Real Estate Services
PNC Bank
Property Sciences Group
Pro-Teck Services
Prudential Financial
Servicelink
Solidifi
Stewart Valuation Services
TrUnion Appraisal Services
Valbridge Property Advisors
Valuation Vision
Weichert Workforce Mobility
Wells Fargo Bank
William Fall Group

05/07/19

Item	*Evaluation*	*Appraisal Report*	*USPAP Cite*
Evaluator must be unbiased	✓	✓	SR 2-3
Evaluator must be independent and have no direct, indirect, or prospective interest, financial or otherwise, in the property or the transaction	✓	✓	SR 2-3 NOTE: USPAP allows an interest if disclosed
Identify the Client		✓	SR 2-2(a)(i)
State the Intended Use		✓	SR 2-2(a)(ii)
Description of the Property, and its Current and Projected Use	✓	✓	SR 2-2(a)(iii) SR 2-2(a)(ix)
State the Interest Being Appraised		✓	SR 2-2(a)(iv)
Estimate property's *market value* in its actual condition, use and zoning as of the effective date, with any limiting conditions	✓	✓	SR 2-2(a)(v) SR 2-2(a)(vi) SR 2-2(a)(viii)
Describe methods used to confirm the property's actual physical condition and the extent to which an inspection was performed	✓	✓	SR 2-3 NOTE: The certification addresses the level of inspection performed and by whom
Describe the analysis that was performed and the supporting information that was used in valuing the property	✓	✓	SR 2-2(a)(vii) SR 2-2(a)(viii)
Explain the exclusion of the sales comparison, cost, or income approaches		✓	SR 2-2(a)(vii)

Item	*Evaluation*	*Appraisal Report*	*USPAP Cite*
Describe the supplemental information that was considered when using an analytical method or technological tool	✓	✓	SR 2-2(a)(viii)
Indicate all sources of information used in the analysis, as applicable, to value the property including: – External data sources (such as market sales databases and public tax and land records); – Property-specific data (such as previous sales data for the subject property, tax assessment data, and comparable sales information); – Evidence of a property inspection; – Description of the neighborhood; or – Local market conditions.	✓	✓	SR 2-2(a)(vii) SR 2-2(a)(viii)
If an opinion of highest and best use was developed, summarize the support and rationale for that opinion		✓	SR 2-2(a)(x)
Clearly and conspicuously state all extraordinary assumptions and hypothetical conditions used, and state that their use might have affected the assignment results		✓	SR 2-2(a)(xi)
Include information on the preparer when an evaluation is performed by a person, such as the name and contact information, and signature (electronic or other legally permissible signature) of the preparer	✓	✓	SR 2-3

§ 323.3 Appraisals required; transactions requiring a state certified or licensed appraiser.

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

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

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

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

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

(5) The transaction is a business loan that:

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

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

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

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

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

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

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

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

(10) The transaction either:

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

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

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

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

(13) The transaction is a commercial real estate transaction that has a transaction value of $500,000 or less.

Attachment 4

Board of Governors of the Federal Reserve System
Federal Deposit Insurance Corporation
Office of the Comptroller of the Currency
National Credit Union Administration

May 17, 2017

Debra Rudd
President
Association of Appraiser Regulatory Officials
13200 Strickland Road
Suite 114-264
Raleigh, North Carolina 27613

Dear Ms. Rudd:

This letter responds to letters from former presidents Nikole Avers and Anne M. Petit, dated August 11, 2015, and June 9, 2016, respectively, to Arthur Lindo, Chairman of the Appraisal Subcommittee (ASC) of the Federal Financial Institutions Examination Council (FFIEC) on behalf of the Association of Appraiser Regulatory Officials (AARO). The questions posed in both letters concern the definitions of "real estate-related financial transaction" and "federally related transaction" in Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (Title XI)[1] and implementing regulations (the Appraisal Regulations), adopted by the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the National Credit Union Administration (NCUA) (collectively, "the agencies").[2] The ASC has referred these letters to the agencies because the letters concern the Appraisal Regulations.

Congress defined the terms "real estate-related financial transaction" and "federally related transaction" in Title XI.[3] The agencies' Appraisal Regulations, consistent with the Title XI definition, define the term "real estate-related financial transaction" as any transaction involving:

(1) the sale, lease, purchase, investment in or exchange of real property, including interests in real property, or the financing thereof;
(2) the refinancing of real property or interests in real property; or
(3) the use of real property or interests in property as security for a loan or investment, including mortgage-backed securities.[4]

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[1] Public Law No. 101–73, Title XI, 103 Stat. 511 (1989); 12 U.S.C. § 3331, *et seq.*
[2] See 59 Fed. Reg. 29482 (June 7, 1994); *see also* 12 C.F.R. Part 225 Subpart G (FRB); 12 C.F.R. Part 323, Subpart A (FDIC); 12 C.F.R. §§ 34.41 – 34.47 (OCC); 12 C.F.R. §§ 722.1 – 722.7 (NCUA).
[3] 12 U.S.C. §§ 3350(4) and 3350(5).
[4] 12 C.F.R. § 34.42(i) (OCC); 12 C.F.R. § 225.62(i) (FRB); 12 C.F.R. § 323.2(i) (FDIC); 12 C.F.R. § 722.2(h) (NCUA).

The Appraisal Regulations also carry forward the Title XI language when defining the term "federally related transaction" (FRT) as any real estate-related financial transaction entered into that (1) the agencies, or any of their regulated institutions engage in or contract for; and (2) requires the services of an appraiser.[5] The Appraisal Regulations include categories of real estate-related financial transactions that do not require the services of an appraiser and thus are not FRTs.[6]

The impact of real estate transactions that would be exempt from the appraisal requirements was discussed in the preamble to the Appraisal Regulations issued in 1994. The preamble stated, "[i]n their appraisal regulations, the agencies identify categories of real estate-related financial transactions that do not require the services of an appraiser in order to protect federal financial and public policy interests or to satisfy principles of safe and sound banking. These real estate-related financial transactions are not federally related transactions under the statutory and regulatory definitions. Accordingly they are subject to neither Title XI of FIRREA nor those provisions of the agencies' regulations governing appraisals."[7]

The Appraisal Regulations provide that a real estate-related financial transaction that "is wholly or partially insured or guaranteed by a United States government agency or a United States government-sponsored agency"[8] is exempted and thus not an FRT. The agencies have clarified that this exemption from the definition is intended to cover only those transactions that meet all underwriting requirements of the federal insurer or guarantor, including its appraisal requirements, in order to receive the insurance or guarantee.[9] Similarly, transactions that qualify for sale to or meet the appraisal standards of a U.S. government agency or U.S. government-sponsored agency are exempted from the Appraisal Regulations and, thus, not FRTs.[10]

While the Appraisal Regulations require appraisals only for FRTs, other requirements apply to transactions that meet an exemption. For example, for real estate-related financial transactions at or below the specified dollar thresholds[11] and certain transactions involving existing extensions of credit,[12] the Appraisal Regulations require banking organizations to obtain

[5] 12 C.F.R. § 34.42(f) (OCC); 12 C.F.R. § 225.62(f) (FRB); 12 C.F.R. § 323.2(f) (FDIC); 12 C.F.R. § 722.2(e) (NCUA).
[6] 12 C.F.R. § 34.43(a) (OCC) 12 C.F.R. § 225.63(a) (FRB); 12 C.F.R. § 323.3(a) (FDIC); 12 C.F.R. § 722.3(a).
[7] 59 Fed. Reg. 29482 (June 7, 1994).
[8] 12 C.F.R. § 225.63(a)(9) (FRB); 12 C.F.R. § 34.43(a)(9) (OCC); 12 C.F.R. § 323.3(a)(9) (FDIC); 12 C.F.R. § 722.3(a)(7) (NCUA).
[9] See *Interagency Appraisal and Evaluation Guidelines*, 75 FR 77450, 77467 (December 10, 2010) ("Interagency Appraisal Guidelines"); 59 FR 29493 – 29494.
[10] 12 C.F.R. § 225.63(a)(10) (FRB); 12 C.F.R. § 34.43(a)(10) (OCC); 12 C.F.R. § 323.3(a)(10) (FDIC); 12 C.F.R. § 722.3(a)(8) (NCUA).
[11] 12 C.F.R. § 225.63(a)(1) and (5) (FRB); 12 C.F.R. § 34.43(a)(1) and (5) (OCC); 12 C.F.R. § 323.3(a)(1) and (5) (FDIC); 12 C.F.R. § 722.3(a)(1) and (5) (NCUA).
[12] 12 C.F.R. § 225.63(a)(7) (FRB); 12 C.F.R. § 34.43(a)(7) (OCC); 12 C.F.R. § 323.3(a)(7) (FDIC); 12 C.F.R. § 722.3(a)(7) (NCUA).

an evaluation consistent with safe and sound banking practices.[13] Regardless of whether or not a real-estate related financial transaction is a FRT, the agencies expect banks to have policies and procedures for conducting and overseeing appraisals and evaluations that are consistent with the *Interagency Appraisal and Evaluation Guidelines*.

For ease of reference, we have attached the final rule for Real Estate Appraisals published in the Federal Register on June 6, 1994, as well as the *Interagency Appraisal Guidelines*.

Should you have any further questions with regard to this issue, please contact FRB: Gillian Burgess, Senior Counsel, Legal Division, (202) 736-5564; FDIC: Mark Mellon, Counsel, Legal Division, (202) 898-3884; OCC: Mitchell Plave, Special Counsel, Law Department, (202) 649-5490; or NCUA: John Brolin, Senior Staff Attorney, (703) 518-6540.

Sincerely,

Arthur Lindo
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Board of Governors of the Federal Reserve System

for MH
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Deputy Comptroller for Credit Risk
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Timothy Segerson
Deputy Director
Office of Examination and Insurance
National Credit Union Administration

Attachments:
Federal Register, *Real Estate Appraisals*, Final Rule, June 6, 1994, pages 29482-29503.
Interagency Appraisal and Evaluation Guidelines, December 10, 2010.

[13] 12 C.F.R. § 225.63(b) (FRB); 12 C.F.R. § 34.43(b) (OCC); 12 C.F.R. § 323.3(b) (FDIC); 12 C.F.R. § 722.3(b) (NCUA).

Why Appraisers Matter

Automated valuation models are tools, not solutions.

By John S. Brenan

Because you may be reading this on a laptop, tablet, or smartphone, you already know that today we use technology in ways we never imagined even a few years ago. Who could have dreamed of ordering something online and having it delivered within hours? Now we're anticipating deliveries via driverless cars and flying drones.

With these advances, will computers inevitably replace appraisers when it comes to valuing homes? That question is the subject of much debate. In some limited transactions, an automated valuation model may be used appropriately today instead of an appraisal. Based on the specifics of the property and the transaction details, an appraisal may be unnecessary. For example, I'd be irate if I owned a $2 million home free and clear but had to pay a large fee for an appraisal in order to take out a $50,000 line of credit. However, if I'm looking to buy a $500,000 home with 10 percent down, is it reasonable for a lender to rely on artificial intelligence to determine whether the collateral is adequate? Not likely.

I couldn't agree more with the sentiments of Karen Belita, a data scientist with the National Association of REALTORS®, who wrote in a blog post, "When it comes to online home value estimates, the number one caveat for consumers is that these estimates are not a substitute for formal appraisals, comparative market analyses, and the in-depth expertise of real estate professionals." Bravo. Indeed, AVMs are not appraisals. It's possible that as technology evolves, AVMs may be used to a greater degree. But today, in many cases, an automated valuation is suspect if there is a lack of available data or the property isn't a "cookie cutter." Many of us have checked our own properties against the finding of an AVM and thought, "Yeah, right." When it comes to AVMs, your mileage may vary.

So why aren't automated models more reliable in more transactions? Because *computers* don't buy houses; *people* do. An AVM does a great job of analyzing tangible features such as a property's age, number of bedrooms and baths, square footage, and lot size. However, a property's overall appeal is something that has been, at least to date, extremely difficult to quantify. It's a uniquely human phenomenon; a property's overall appeal reflects a combination of characteristics. While not everyone has the same preferences, some unusual features will likely face significant market reluctance.

But wait, you say, aren't appraisers required by the Uniform Standards of Professional Appraisal Practice to be "independent, impartial, and objective"? Absolutely. Still, appraisers are not machines. They must have relevant data and logic to support their analyses, opinions, and conclusions, but they also incorporate the concept of market value reflecting the interests of consumers who are "typically motivated" and "well-informed."

Recognizing that AVMs play a role in developing an appraisal, the authors of USPAP acknowledge their relevance with respect to their use of regression, adaptive estimation, neural network, expert reasoning, and artificial intelligence. But appraisers remain better than AVMs at recognizing motivations and knowledge levels of market participants.

The output of an AVM is not, by itself, an appraisal. It may become a basis for one if the appraiser believes the output to be credible for use in a specific assignment. *If the appraiser believes it to be credible.* Today, that's a very big "if." So unless and until AVMs can better emulate the human factor an ethical and competent appraiser remains indispensable.

As published in REALTOR Magazine, September-October, 2018 and accessible at: https://magazine.realtor/news-and-commentary/commentary/article/2018/09/why-appraisers-matter

REVAA
Real Estate Valuation Advocacy Association

Testimony by Jeff Dickstein
Chief Compliance Officer
Pro Teck Valuation Services

On Behalf of the
Real Estate Valuation Advocacy Association (REVAA)

Before the
House Committee on Financial Services
Subcommittee on Housing, Community Development and Insurance

Hearing on
"What's Your Home Worth? A Review of the Appraisal Industry."

Thursday, June 20, 2019

Introduction

Good afternoon Chairman Clay, Ranking Member Duffy, and members of the Subcommittee. Thank you for the privilege to share the perspective of appraisal management companies (AMC) at the Subcommittee on Housing, Community Development and Insurance hearing entitled, *"What's Your Home Worth? A Review of the Appraisal Industry."*

Since the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) nearly a decade ago, the appraisal industry has changed significantly as Congress intended to protect safety and soundness. There has been much progress made and ample room for improvement.

The following submitted testimony from the Real Estate Valuation Advocacy Association (REVAA) seeks to respond to the questions posed by the Subcommittee. It is also intended to provide insight into the appraisal industry from the perspective of appraisal management companies (AMC), many of which also serve as a lender valuation provider beyond residential appraisals. Specifically, this testimony addresses the items below:

- An overview of the role of AMCs in the residential mortgage process;
- The AMC state regulatory structure post Dodd-Frank Act;
- Support for the recruitment and training of the next generation of residential real estate appraisers;
- Integrating human capital, data and technological innovation in the appraisal industry;
- Undervaluation of properties in minority neighborhoods; and
- Suggested next steps for Congress and the industry.

About Appraisal Management Companies

AMCs are third party service providers engaged by bank/non-bank lenders to work with appraisers on residential appraisals in compliance with federal appraisal independence requirements. AMCs have existed since the 1960's and were primarily utilized by the largest US financial institutions to reduce consumer costs by outsourcing the expenses that would be incurred through their internal management of the valuation process. AMCs grew in popularity among smaller and mid-size lenders following the 2010 financial crisis as their attention to efficiency, compliance and regulatory responsibilities helped ensure consumer protection. The outsourcing of the valuation process continued, extending to the largest financial institutions, who now rely upon AMCs for the valuations of residential mortgages. Today, there are an estimated 300-400 AMCs in the nation, ranging from small local businesses to large national corporations.

AMCs benefit consumers by ensuring that the residential property they are purchasing, refinancing, or otherwise using as collateral is properly evaluated and that the lender they are working with to secure their residential mortgage transaction will receive a quality, timely appraisal that is reasonably priced based on current market conditions, free from undue influence, and compliant with the *Uniform Standards of Professional Appraisal Practice* (USPAP). Among an AMC's core functions include:

- Maintaining a panel of qualified appraisers ready to execute lender valuation assignments.
- Ensuring appraiser independence by safeguarding against fraud and undue influence.
- Providing quality assurance processes in the delivery of final appraisal and valuation products.
- Supporting a smooth, timely and responsive mortgage process for consumers and lenders.
- Ensuring lender compliance with federal and state banking and mortgage regulations.

AMCs invest significantly in technology to support the above functions, including but not limited to developing proprietary ordering processes that can integrate with appraisal form provides and other real estate technology solutions and implementing automated quality control rule sets. It is important to underscore that the AMC's lender customer sets the expectations for how an AMC must manage its appraisal orders – this is critical as there is a misunderstanding amongst appraisers that AMCs set appraisal order turn times, delivery requirements, and other obligations.

In addition, many AMCs are more appropriately described as valuation providers that often provide customers with a variety of valuation-related products and management services, including but not limited to evaluations, broker price opinions, automated valuation models, property data collection products, post-disaster property reviews, and data analytics. While a business may meet the definition of an AMC, they often provide many other services - this business model is beneficial to customers, borrowers, and helps to support a more healthy and cohesive process.

Lenders, mortgage companies, investors, government-sponsored entities and others seek different levels of service from a valuation company for several reasons, including:

- Valuation companies are experts in real estate property data. Customers seek to work with companies that have expertise in all real estate collateral risk concepts.
- From a vendor management perspective, customers demand to work with one business that can support many needs, as opposed to working with an AMC, a valuation company, and data company. This helps banks and other regulated industries more effectively provide much more effective oversight of their vendors.
- Valuation companies invest heavily in technology, product development tools, vendor panels to be able to adapt to shifts in the marketplace, which provides economies of scale and efficiencies to support customer needs for different transaction types.

Under federal law and regulation, lender clients may be held responsible for the actions or inactions of their third-party vendors, including AMCs. Therefore, AMCs are under continuous, vigorous, and extensive scrutiny by their lender clients through the lender client third-party oversight programs. AMCs are required to regularly submit to client audits to ensure compliance with federal banking regulations and lender policies and procedures. In addition, lender transactions with AMCs are regulated by state and federal banking regulators.

Fannie Mae, Freddie Mac and others have praised the role AMCs have played in improving appraisal quality and enforcing federal Appraisal Independence Requirements (AIR) since the Home Value Code of Conduct (HVCC) and Dodd-Frank were enacted. In addition, AMCs are actively involved in the non-profit and for-profit advisory councils of The Appraisal Foundation ("TAF"), many of their representatives have sat on the TAF Appraiser Qualifications Board and Appraisal Standards Board and participate in meetings hosted by The Association of Appraiser Regulatory Officials ("AARO").

AMC Oversight Post Dodd-Frank Act

The Dodd-Frank Act was rooted in the objective to restore public trust in the safety and soundness of the financial industry. Specific to appraisal and AMCs, Dodd-Frank adopted several important consumer protections that REVAA supports, including but not limited to:

- The Truth in Lending Act ("TILA") was amended to make it unlawful, in extending credit or in providing any services for a consumer credit transaction secured by the principal dwelling of the consumer, to engage in any act or practice that violates appraisal independence.
- The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") was amended to include AMCs within the scope of appraisal activity overseen by the Appraisal Subcommittee and applicable federal regulators.

Supporting Appraiser Independence Under TILA

- *Safeguard Appraiser Independence and Protecting Against* Fraud - AMCs help ensure that appraisals are completed in compliance with federal and state laws, as well as industry standards (USPAP), and that appraisers form their value opinions independently, without undue influence. Preventing coercion is critical to avoiding collusion in the valuation process and thereby reducing the potential for fraud.

- *Protect Public Safety* - Consumers are provided an extra layer of safety and protection as most AMCs are required to conduct background checks before appraisers are employed or empaneled. Further, AMCs continue to monitor appraisers on an ongoing basis to ensure that appraisers who are unqualified or may pose a threat to public trust or safety are removed.

- *Ensure Lender Compliance with State and Federal Banking and Mortgage Regulations* - AMCs are invaluable partners for lenders as they ensure efficiency and support lender compliance with the mortgage lending requirements of state and federal regulators (e.g., Fed, FDIC, OCC, CFPB).

- *Ensure Appraiser Independence* - Lenders (big banks, small banks, mortgage lenders, credit unions, etc.) use AMCs because they provide efficient solutions to establish and maintain the necessary firewalls to preserve appraiser independence. Lenders require that AMCs maintain processes to give appraisers a clear path to complain if they believe they are being unduly influenced.

- *Ensure Quality Essential to Consumers and the Secondary Market* - AMCs provide the quality assurance lenders need to ensure a valuation won't prevent a loan from being saleable in the secondary market. Federal agencies require lenders to provide thorough, accurate, and objective appraisal reports with reliable opinions of market value to support underwriting decisions.

With respect to possible confirmation bias where an appraisal confirms or exceeds the associated contract price, we do not believe confirmation bias is tied to appraiser independence. Specifically:

- To the extent an appraiser believes that a subject property is valued within an acceptable range of the contract price, it is extremely common for the appraiser to decide on the contract price as the final opinion of value;

- Price confirmation and overvaluation should not by themselves be indicators of appraisal quality or appraiser independence, as such metrics are based on a number of market factors, and the ultimate determination of quality is based on whether the opinions of value are credibly supported.

- Studies of price confirmation often review years in which home price appreciation was strong and healthy – it is possible that appraisals often met or slightly exceeded purchase prices during the more recent sampling, as market conditions could cause prices to rise between a property's contract agreement and eventual appraisal. Moreover, post-recession sale of foreclosed property by financial institutions may have contributed to more overvaluation and super-overvaluation.

- An arm's length transaction where both buyer and seller are each acting in their own best interest, the sale price they negotiate is likely to be a direct reflection of market value.

- Additional testing and evaluation of appraisal values is needed to better understand possible confirmation bias.

Ultimately, while confirmation bias could be an indicator of appraiser independence, we believe these are two separate issues.

FIRREA – Guidance for State Regulation of AMCs

The Dodd-Frank amendments to FIRREA and their subsequent regulations promulgated after Dodd-Frank's enactment created the path for States to register AMCs providing appraisal management services related to a federally related transaction. The Board of Governors of the Federal Reserve System, the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the National Credit Union Administration Board, the Federal Housing Finance Agency, and the Bureau of Consumer Financial Protection (collectively, "the Federal Banking Regulators") were tasked to jointly, by rule, establish minimum requirements to be applied by a State in the registration of appraisal management companies.

These minimum rules became effective on August 10, 2015. FIRREA provides that no appraisal management company may perform services related to a federally related transaction in a State after the date that is 36 months after their rules' effective date, unless such company is registered with such State or subject to oversight by a Federal financial institution regulatory agency. There was also an opportunity for States to obtain a one-year extension from the Appraisal Subcommittee - the firm deadline is now August 10, 2019.

Pursuant to the minimum rules, at minimum a State registration program must include a requirement that AMCs:

- register with and be subject to supervision by a State appraiser certifying and licensing agency in each State in which such company operates;
- verify that only licensed or certified appraisers are used for federally related transactions;
- require that appraisals coordinated by an appraisal management company comply with the Uniform Standards of Professional Appraisal Practice; and
- require that appraisals are conducted independently and free from inappropriate influence and coercion pursuant to the appraisal independence standards established under section 129E of the Truth in Lending Act.

The Appraisal Subcommittee is authorized to review State AMC program compliance with the above requirements.

Seeking to ensure that there was appropriate oversight over AMCs, many States passed AMC registration programs – REVAA has been actively engaged in supporting the registration and oversight of AMCs in all States.

A total of 49 states have implemented AMC registration programs consistent with federal law and rules. In Massachusetts, legislation is proceeding and expected to pass. The only U.S. states and jurisdictions that are poised to opt-out of enacting these important Dodd-Frank consumer protections are the District of Columbia, Puerto Rico, Guam, Virgin Islands and the Northern Marianas Islands.

As a result, AMCs are now state regulated and under significant regulatory scrutiny. They must comply with a number of important requirements, including but not limited to:

- Only engaging with appraisers who have an active appraiser credential in good standing;
- Requiring disclosure of its registration number to appraisers when ordering appraisals;
- Not employing persons who have had appraiser credentials revoked;
- Disclosing to customers fee information about completed appraisals;
- Maintaining a process to require that an appraiser comply with USPAP and state law;
- Paying appraisers within a defined period of time;
- Maintaining a process for reviewing the work of appraisers;
- Informing regulators of address changes or material changes in ownership
- Maintaining a surety bond;
- Being subject to audit by state regulators

Violations of any of these requirements may result in disciplinary action by the state regulators.

REVAA supports the Dodd-Frank amendments to FIRREA and believes that proper oversight by federal and state regulators over AMCs is critical to supporting a health valuation marketplace and ensuring safety and soundness of financial institutions. Therefore, we continue to support AMC registration by all 50 states and the five U.S. territories to strengthen and ensure consistent appraiser independence and consumer protections across the entire United States.

AMC National Registry

As part of the amendments to FIRREA, each State was given authority to collect a fee from AMCs to transmit to the Appraisal Subcommittee to pay for the ASC's oversight efforts, including maintaining a roster of AMCs registered in States (the "AMC Registry"). The amount of the fee is set in statute, and is as follows:

- For an AMC that has been in existence for more than a year, $25 multiplied by the number of appraisers working for or contracting with such company in such State during the previous year, but where such $25 amount may be adjusted, up to a maximum of $50, at the discretion of the Appraisal Subcommittee, if necessary to carry out the Subcommittee's functions under this title; and

- For an AMC that has not been in existence for more than a year, $25 multiplied by an appropriate number to be determined by the Appraisal Subcommittee, and where such number will be used for determining the fee of all such companies that were not in existence for more than a year, but where such $25 amount may be adjusted, up to a maximum of $50, at the discretion of the Appraisal Subcommittee, if necessary to carry out the Subcommittee's functions under this title.

States must collect this fee from registered AMCs no later than June 1, 2020, and many States have already begun collecting the fee. We believe the current feel calculation is problematic for a number of reasons:

- The above is a huge burden to AMCs. The annual cost of this new registry fee is anticipated to range as high as $150,000 or more per year for AMCs that work on a national basis.

- This fee will be a real financial burden on mid- to small-sized AMCs just trying to compete for survival, which will result in reduced competition in the valuation market.

- More money is being collected than is needed to operate an AMC Registry. Dodd-Frank required the creation of the AMC Registry, along with the assessment and collection of this fee. Because of the flawed funding formula, the Appraisal Subcommittee will collect millions more than is actually needed that will then be granted back to states to subsidize their appraisal management programs.

- Because the above funding formula is in Dodd-Frank, we are aware of no other option for relief other than revising the statute.

REVAA supports legislation to amend the above fee to grant the Appraisal Subcommittee discretion to amend the fee if it determines the fees result in adverse consequences or are otherwise not appropriately tailored to meet the ASC's goals. We also support the ASC issuing a report to Congress justifying its decision before any change would occur.

Support for the Recruitment and Training of New Appraisers

National demographic data has long forecasted the coming retirement of the nation's Baby Boom generation and the profound impact to American businesses as industries experience a shortage of available skilled workers. The U.S. Census Bureau estimates that by 2025, the population of people 65 and older will increase by 37.8%, while the population of those 18 to 64 will rise by only 3.2%. Persons aged 18 to 24 will decrease in number.[1]

Following national trends, certified residential appraisers are aging and leaving the workforce. According to a recent Appraisal Qualifications Board "Practice Analysis Survey:"[2]

- 70% of the 2,066 respondents were 51 years or older
- Of those, 30% were 66 years or older
- Only 13% of the respondents were 40 years old or younger

[1] Jennifer M. Ortman, Victoria A. Velkoff, and Howard Hogan, "An Aging Nation: The Older Population in the United States," May 2014, , https://www.census.gov/prod/2014pubs/p25-1140.pdf.
[2] Appraiser Qualifications Board, "Practice Analysis Survey," 2014.

Beyond aging, there are other challenges facing appraisers including:

- Dwindling number of new appraisers - There is a shortage of young adults, graduates and those in career transition seeking to become appraisers.

- Lack of appraisers that want to be supervisors - Supervisory appraisers are hesitant to want to take on the responsibility or economic burden of training.

- Burdensome licensing requirements - It's not easy for new people entering the industry to become an appraiser. Appraisal Licensing/Certification requirements are exhaustive, time intensive and often economically infeasible

- Not all credentialed appraisers are practicing in the field - According to the Appraisal Subcommittee National Appraiser Registry, as of October 2018 there were a total of 94,678 Certified Appraisers in the United States and five territories (48,114 Certified Residential Appraisers, 39,084 Certified General Appraisers, and only 7,480 Licensed Appraisers). However, a large number of credentialed appraisers may not actually be appraising residential properties in the field.

- Lender resistance to use of trainees - Because trainees are not on the National Registry, many lender risk-management policies and procedures restrict, limit or prohibit the use of trainees.

REVAA supports several collaborative industry initiatives to make a real difference in attracting and training the next generation of real property appraiser, including:

- The Appraisal Foundation Appraisal Qualifications Board's new education and experience requirements for new appraisers entering the field, along with the creation of the Practical Applications of Real Estate Appraisal (PAREA) to provide voluntary guidelines for trainee programs to ensure they are eligible for experience credit.

- Industry efforts to recruit military veterans and other people to consider becoming appraisers. There is nothing that discriminates against persons of all backgrounds, gender, race, religion or ethnicity to be an appraiser if they complete the applicable education and experience requirements.

- AMCs and lenders have become more instrumental in providing supervisory training to new appraisers.

- AMCs continue to encourage lenders to allow appraiser trainees to work on assignments when possible, including developing new trainee programs.

- The introduction of H.R. 2852 and S.1722, which would permit licensed real estate appraisers to perform FHA appraisals – led by the Appraisal Institute and The Appraisal Foundation – is important as it would allow more appraisers practicing in the field today to be eligible to conduct real estate evaluations on FHA properties.

- REVAA is proud to work with the House Financial Services Committee, Appraisal Subcommittee and other stakeholders to support soon to be introduced legislation to add appraiser trainees to the National Appraiser Registry.

Collectively, the efforts above and others will make a positive impact in attracting new future appraisers.

Integrating Human Capital, Data and Technological Innovation

With growing calls for modernization by policymakers, consumers, lenders, investors and others, dynamic new technologies and the availability of decades worth of property data have generated excellent potential to innovate residential appraisals and valuations to support more effective and efficient opportunities to evaluate collateral risk while still ensuring the quality of those products meets industry expectations.

Along with modernization, REVAA supports a vibrant appraiser industry because the future isn't going to solely rely on new technology and data. We feel strongly that the future of appraisal needs to retain a human component, which is why we support the recruitment of new appraisers to help revitalize the professional for the next generation. The reliance on appraisers and appraisal products creates an important need to help ensure the sustainability of the profession. Consumers, residential mortgage lenders, secondary markets and AMCs rely on a plentiful supply of qualified appraisers to meet anticipated demand.

Therefore, we believe that the modernization efforts above will not replace appraisers but will complement the appraiser's essential role in utilizing their experience, education, local market knowledge to analyze a subject property and develop a credible opinion of value. Beyond appraisals, there are a wide variety and range of valuation products that can be available to financial institutions, mortgage companies, investors, and others making real estate collateral decisions. The following are several examples:

Evolving Use of Automated Valuation Models.

An automated valuation model ("AVM") is defined in FIRREA as "any computerized model used by mortgage originators and secondary market issuers to determine the collateral worth of a mortgage secured by a consumer's principal dwelling."[3]

AVMs are used in a number of different contexts, including but not limited, for: (1) assess collateral value before deciding what type of additional valuation is required; (2) valuing a portfolio; (3) for lending decisions where an appraisal is not required (i.e., for home equity lending purposes). Federal guidelines define how an AVM can be used in lieu of an appraisal as prescribed by the Interagency Appraisal and Evaluation Guidelines.

Importantly, not all AVMs built the same. There are consumer-facing AVMs that provide value estimates for various non-lending purposes, and lending-grade AVMs that have sufficient data and analysis to support lending use.[4] Testing of AVMs can also vary.[5]

REVAA supports the use of AVMs for permitted purposes, but we recognize that AVMs are not appropriate in all cases for lenders to make collateral valuation decisions – we recognize and appreciate an AVM in a market-data rich neighborhood for a traditional property may be more effective than an AVM in a market with little data and for an atypical property. As with any valuation tool, the loan-type, loan-to-value ratio of the transaction, whether the property is atypical for its neighborhood, and data availability all could impact whether an AVM should be relied on exclusively in making a lending decision.

Federal Banking Regulators were tasked under the Dodd-Frank amendments to FIRREA to promulgate regulations to implement AVM quality control standards, including standards designed to:

1) ensure a high level of confidence in the estimates produced by automated valuation models;
2) protect against the manipulation of data;
3) seek to avoid conflicts of interest;
4) require random sample testing and reviews; and
5) account for any other such factor that the agencies listed in subsection (b) determine to be appropriate.[6]

We welcome that guidance so long as it does not interfere with marketplace competition and the responsible use of these products.

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[3] 12 U.S.C. 3354(c).

[4] Mortgage Bankers Association, "Real Estate Appraisals [RIN: 1557-AE57; 3064-AE87; 7100-AF30],"
https://www.mba.org/Documents/MBA_Real_Estate_Appraisals_(0).pdf

[5] "A Lender's Guide to the Top 3 AVM Testing Methods," ClearCapital.com, Inc, June 06, 2019,
https://www.clearcapital.com/blog-avm-testing-guide/.

[6] 12 U.S.C. 3354(a), (b).

Growing Interest in "Hybrid" Appraisal Products.

Concern over appraiser availability, higher residential appraisal costs and long turn times in some major U.S. housing markets in 2016 and 2017 may have subsided for now. However, lenders and consumers in rural areas continue to feel the strain from a lack of supply of credentialed appraisers. A product that has received attention recently is called a "hybrid" appraisal, where a third-party collects data about a property, and an appraiser prepares an analysis and opinion of value using that third-party information. Such products are not new - but they have received new interest for issuance of home equity loans and in the portfolio servicing space.[7]

These valuation products can also significantly help for transactions when an appraisal is not required or in rural areas where turn times and appraiser availability is an issue. We also note that legislation recently passed the Congress (H. 299) authorizing the Department of Veterans Affairs to consider these valuation products.

There is significant confusion by appraisers that these products are being used because they are the cheapest or fastest without consideration for the underling risk of the collateral – this is not the case. Similar to the use of AVMs, a "hybrid" appraisal is appropriate in certain lending situations and not in others.

We encourage further discussion with members of the subcommittee to provide more information on these products.

GSE Evaluation of Appraisal Forms.

Fannie Mae and Freddie Mac established a Uniform Appraisal Dataset ("UAD") Working Group to collect feedback from stakeholders and begin the process to overhaul the uniform appraisal forms to establish a more flexible, dynamic structure for appraisal reporting.[8] Many AMCs members are active participants in the working group and are offering their technology and valuation management expertise.

GSE Evaluation of Property Data.

As part of its appraisal modernization initiative, Fannie Mae announced it is working independently on modernization of the appraisal process, including testing a variety of technologies and methodologies that could enhance our ability to manage collateral risk and make the process more efficient for lenders, borrowers, appraisers, and investors. One of those tests is evaluating alternatives to obtain relevant data about subject properties. Should an appraisal be required to properly evaluate collateral, the test would involve performing a desktop appraisal informed by the data collected about the property.[9] We understand there are AMCs participating in this testing.

Proposed Increase to Residential Appraisal Threshold.

The Subcommittee has asked about the recent proposed regulations from the federal financial institutions regulatory agencies to increase the de minimus threshold at or below which appraisals would not be required for residential real estate-related transactions from $250,000 to $400,000.

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[7] National Association of Realtors, "Are Hybrid Appraisals Becoming the New Normal In Real Estate Transactions?" PR Newswire: Press Release Distribution, Targeting, Monitoring and Marketing, May 15, 2019, https://www.prnewswire.com/news-releases/are-hybrid-appraisals-becoming-the-new-normal-in-real-estate-transactions-300850871.html.

[8] Fannie Mae and Freddie Mac, "Uniform Appraisal Datatset Executive Summary," Uniform Mortgage Data Program, December 2018, https://www.fanniemae.com/content/news/uad-executive-summary.pdf.

[9] Fannie Mae, "Appraiser Update," March 2019, https://www.fanniemae.com/content/news/current-appraiser-newsletter.pdf.

However, as an agent of the lender for appraisal and valuations services and its role in working with independent fee appraisers to complete appraisals, REVAA does not have a position on this proposed change. However, as reflect in our comments to the proposal[10]:

- REVAA members support the Truth in Lending Act and the requirements for valuation independence.
- Limited information available on the cost of evaluations and appraisals suggests material cost savings in connection with real estate property valuation for regulated institutions and consumer, with evaluations costing approximately 20-50% of an appraisal.
- REVAA broadly estimates that finding a qualified professional (e.g., broker, agent, appraiser) to perform an evaluation can be much faster than having to solely rely on an appraiser, particularly in rural areas, with evaluations taking between one to give days vs. five to twenty-one for an appraisal.
- REVAA membership typically do not see evaluations being used in a full loan origination, and even if they could we support an appropriate and more comprehensive valuation product based on the risk of the underlying transaction, not simply whether a threshold amount has been met.
- The estimates above are based on similar products comparison, geographic market, and other variables.

Other Technologies to Support Appraisal and Valuation Efficiency

In addition to the variety of technological enhancements above, REVAA members and others are developing new technology that supports the appraiser and valuation profession. As stated by the Bureau of Labor Statistics, the expectation of greater use in mobile technology will improve efficiencies and productivity.[11] REVAA members believe their investments in technology will transform the profession into a true 21st century expertise. Examples include:

- Mobile applications that allow an appraiser to more accurately measure property and develop a sketch of a residence;
- Scheduling applications that give the borrower better command over scheduling their appraiser / inspector visit which can reduce delays and improve communications between the appraiser and lender; and
- Continued integration of third-party real estate data available at an appraiser's fingertips.

Undervaluation of Properties in Minority Neighborhoods

REVAA appreciates the opportunity to review the November 2018 report by the Metropolitan Program at Brookings.[12] The information has been shared with our members and we continue to review and assess the conclusions in the report.

We believe it is important to underscore that the practice of appraisal requires the historical review and analysis of subject property sales data in similar neighborhoods (i.e., comparables).

AMCs implement varying controls to ensure appraisers (and AMCs) do not engage in discriminatory behavior, including but not limited to the following:

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[10] Real Estate Valuation Advocacy Association, "Comment Request: Docket ID OCC-2018-0038," https://www.regulations.gov/contentStreamer?documentId=OCC-2018-0038-0539&attachmentNumber=1&contentType=pdf

[11] Bureau of Labor Statistics, "Appraisers and Assessors of Real Estate: Occupational Outlook Handbook," https://www.bls.gov/ooh/business-and-financial/appraisers-and-assessors-of-real-estate.htm#tab-6.

[12] Andre Perry, Jonathan Rothwell, and David Harshbarger, "The Devaluation of Assets in Black Neighborhoods," Https://www.brookings.edu/wp-content/uploads/2018/11/2018.11_Brookings-Metro_Devaluation-Assets-Black-Neighborhoods_final.pdf, November 2018.

- Developing policies, procedures, and training that explain fair lending practices and what type of conduct is prohibited;
- Reviewing appraisal reports for possible discriminatory language; and
- Maintaining complaint management programs to investigate borrower complaints alleging discrimination.
- Where appropriate or legally required, AMCs may obtain diversity information from their appraiser panel in accordance with a customer contractual obligation.

REVAA strongly supports and would be willing to partner in efforts to help sustain and diversify the appraiser profession. In particular, we would be interested in partnering with the authors to review if AVM technology could be helpful in better understanding the discrepancies in property valuation in such neighborhoods.

Requirement to Disclose Appraisal Fees

REVAA generally does not take a position regarding amending the Real Estate Settlement Procedures Act (RESPA to require disclosure in the integrated disclosure for mortgage loan transactions of the fee paid directly to the appraiser by an AMC and the administration fee charged by the AMC. However, we offer preliminary feedback that may assist further discussion of this important issue:

- Separating a management fee from the appraisal fee is inconsistent with other fees that are routinely combined for practical business purposes. Other closing services have multiple cost factors (employees, contractors, technology costs) that are not disaggregated – for example, property survey costs do not detail amounts paid to technicians that perform on-site services.
- True disclosure of all cost components of an ordered appraisal may not simply be the appraisal fee and the appraisal management fee. Other costs associated with an appraisal order include, but are not limited to, platform fees, invoice fees, technology fees, and other costs. In other words, the AMC-retained fee is not the AMC's profit.
- The current appraisal fee disclosure offers flexibility for defining the appraisal fee and appraisal management fee, which allows for changes in either should a subject property be determined to be more complex requiring a higher fee to the appraiser. A change could require the lender to provide a new disclosure, resulting in delay to a lending transaction.
- While we defer to lenders and others directly impacted by such a proposal, we note that requiring this fee split could result in other delays in transactions to ensure the lender is properly disclosing the information.
- Borrowers reviewing the disclosure form may be confused over understanding the fee differences.
- A significant majority of states regulating AMCs either: (i) require an AMC to report all fee split information to its customer; (ii) prohibit an AMC from restricting the appraiser's disclosure of their fee in an appraisal report; or (iii) require an appraiser to include in the appraisal report their fee and the AMC's fee.

Related to above point concerning borrower information, we note that the Consumer Financial Protection Bureau in 2013 issued its final rule regarding the integrated mortgage disclosures under RESPA and TILA. In issuing its final rule the CFPB did consider requiring disclosure of the appraiser fee and AMC-retained fee. While the Bureau acknowledged RESPA did not require the disclosure, the CFPB stated:

> It is unclear from [comments submitted by interested parties], however, that a breakout of the AMC's charge from the appraisal would or could lead to the stated result sought by the commenters: that a consumer would utilize the different charges to question and seek an appraisal directly from an appraiser, rather than through the use of an AMC. The Bureau is not aware of any data or information supporting the commenters' belief that this disclosure would achieve their desired results, nor did the commenters supply any such data or information.
>
> Appraisals are third-party reports prepared for the benefit of the creditor as part of an evaluation of the value of the collateral being secured by the property. RESPA recognizes that creditors are the parties that are obtaining the service, and explicitly provides an exemption from constraints on requiring the use of an

> affiliate for appraisals. In addition, many of the concerns identified by commenters have been the subject of other rulemakings directly concerning disclosures and information provided to the consumer in relation to appraisals, namely the 2013 ECOA Appraisals Final Rule and the 2013 Interagency Appraisals Final Rule.
>
> The Bureau believes that, absent data or other information supporting the commenters' beliefs, it would be inappropriate to use its authority to modify the statutory disclosure provision of Dodd-Frank Act section 1475, because requiring breakouts of such charges to be disclosed in all cases may tend to produce information overload.[13]

We believe additional discussion and research may be warranted, particularly with the lending community, to understand the benefits and consequences of imposing this new requirement on lenders and changing the disclosure process, particularly during the current real estate market and other ongoing reforms being considered to the lending process.

Conclusion

The Dodd-Frank Act enacted statutory and regulatory changes to implement new consumer protections. REVAA believes that the systems and structures that have been put in place across the country have largely helped achieve the goal of protecting safety and soundness. But the work isn't done. Despite the great amount of progress that has been made there continues to be a need for industry-wide focus on improvement.

Stakeholders continue to come together to discuss the future of the industry including the recruitment of new appraisers and the appropriate role of new technologies and data on residential appraisal and lender valuations. This constructive dialogue and collaboration must continue. In supporting these efforts, REVAA respectfully requests that Congress:

- Pass H.R. 2852 – the Homebuyer Assistance Act of 2019 to permit licensed real estate appraisers to perform FHA appraisals (along with its companion S. 1722).
- Pass legislation to permit States to report appraiser trainees to the Appraisal Subcommittee Appraiser Registry to support broader use of trainees by lenders.
- Pass legislation to grant regulatory flexibility to the Appraisal Subcommittee so it may adjust AMC fees and promote greater competition in the AMC market.
- Support the registration and oversight of AMCs in all States, territories, and the District of Columbia to promoted appraiser independence and consumer protections.
- Support continued dialogue with federal regulators on opportunities to streamline outdated valuation policy to provide flexibility in the collateral valuation process while ensuring safety and soundness.

Biography of Jeff Dickstein, Chief Compliance Officer, Pro Teck Valuation Services

Jeff Dickstein is a Certified Residential Appraiser with than 37 years of experience in the mortgage industry, including 30 as an appraiser. He currently holds an appraiser credential in 17 states. As Chief Compliance Officer at Pro Teck Valuation Services, a national appraisal management and lender valuation services provider, Dickstein is responsible for company compliance with all state, federal and industry regulations.

Dickstein's diverse background and problem-solver mentality give him a unique perspective on asset valuation, risk mitigation and the future of the industry. He is a past president and current board member of REVAA (Real Estate Valuation Advocacy Association), a national trade organization representing AMCs. Dickstein serves on the Board of Trustees of The Appraisal Foundation and is a past chair of its Industry Advisory Council. He is also a member of CRN (Collateral Risk Network), NAA (National Association of Appraisers) and NAR (National Association of Realtors),

About REVAA

REVAA is an industry trade association whose membership includes AMCs and lender valuation providers that collectively provide residential valuation transaction volume nationwide on behalf of mortgage lenders. In addition, many REVAA members also provide other important lender valuation services such as Broker Price Opinions (BPO) and Alternative Valuation Methods (AVM).

[13] 78 FR 80225, pp. 79955-79956 (internal citations omitted).

BROOKINGS

QUALITY. INDEPENDENCE. IMPACT.

Know Your Price: The Devaluation of Residential Property in Black Neighborhoods

Testimony Submitted to U.S. House of Representatives Committee on Financial Services
Subcommittee on Housing, Community Development and Insurance

"What's Your Home Worth? A Review of the Appraisal Industry"

Andre M. Perry
David M. Rubenstein Fellow
Metropolitan Policy Program
The Brookings Institution
June 20, 2019

Chairman Clay, Ranking Member Duffy, and Ranking Member Gooden,

Thank you for inviting me to testify today *on this extremely important issue that affects millions of people across this country.*

Homeownership lies at the heart of the American Dream, representing success, opportunity, and wealth. However, for many of its citizens, America deferred that dream. For much of the 20th century, the devaluing of black lives led to segregation and racist federal housing policy through redlining that shut out chances for black people to purchase homes and build wealth, making it more difficult to start and invest in businesses and afford college tuition. Still, homeownership remains a beacon of hope for all people to gain access to the middle class.

Compared to investing in the stock market and other ways to grow a nest egg, homeownership is still the most consistent and accessible way to build wealth over time. And while homeownership rates vary considerably between whites and people of color, it's typically the largest asset among all people who hold it, regardless of race. If we can detect how much racism depletes wealth from black homeowners, we can begin to address bigotry principally by giving black homeowners and policymakers a target price for redress. Laws have changed, but the value of assets—buildings, schools, leadership, and land itself—are inextricably linked to the perceptions of black people. And those negative perceptions persist.

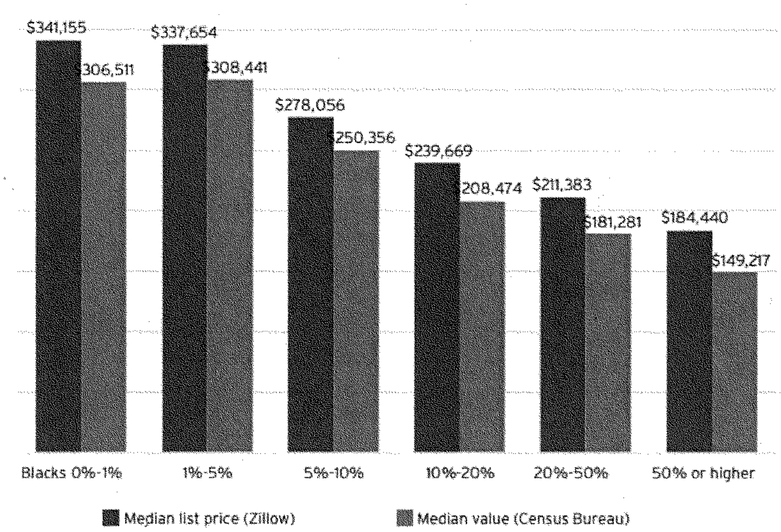
Through the prism of the real estate market and homeownership in black neighborhoods, the research of myself and my colleagues Jonathan Rothwell at Gallup, and David Harshbarger at Brookings, addressed the question: What is the cost of racial bias? We sought to understand how much money majority-black communities are losing in the housing market stemming from racial bias, **finding that owner-occupied**

homes in black neighborhoods are undervalued by $48,000 per home on average, amounting to $156 billion in cumulative losses.

FIGURE 1

Neighborhood median home value by black population share

U.S. metropolitan areas, 2012-2016



Source: Authors' analysis of Zillow and 2016 American Community Survey 5-year estimates

We've known for some time that racism limited blacks' housing options in ways that lowered the value of homes. De jure and de facto segregation — racially restrictive housing covenants that prohibited blacks from buying in certain areas throughout the 20th century — and racially biased redlining from the 1930s beyond the passage of the Fair Housing Act of 1968 — which deemed majority-black neighborhoods too risky for mortgage lenders — isolated blacks in areas that realized lower levels of investment than their white counterparts.

There is strong evidence that bias has tangible effects on real estate markets, both historically and today. During the 20th century, both explicit government institutions and decentralized political actions created and sustained racially segregated housing conditions in the United States.[i] This has created what has been dubbed a "segregation tax," resulting in lower property valuations for blacks compared to whites per dollar of income.[ii]

Contemporary work from social scientists has aimed to sort out whether these lower valuations are caused by differences in socio-economic status, neighborhood qualities, or discrimination.[iii] The results tend to show compelling evidence for discrimination.[iv] In one study, Valerie Lewis, Michael Emerson, and Stephen Klineberg collected detailed survey data on neighborhood racial preferences in Houston, Texas. They asked people to imagine that they were looking for a new house, found one within their price range and close to their job; they then say to respondents, "checking the neighborhood . . ." and then present difference scenarios based on racial composition, school quality, crime, and property value changes for the hypothetical neighborhood." Consistent with previous research, they find that these neighborhood features strongly predict whether someone says they would buy the house. Racial composition strongly predicted the preferences of whites in neighborhoods that were otherwise identical.

Researchers Jacob Fabera and Ingrid Gould Ellen examined the variation of rising housing prices among people of different racial categories who purchased their homes before the boom from 2000 to 2007 and kept them through the bust of 2008.[v] They found that blacks and Hispanics gained less equity than whites during that period and were more likely to owe more than their home was worth. The researchers found that "[b]lack–white gaps were driven in part by racial disparities in income and education and differences in types of homes purchased." They hypothesized that racial segregation and the corollary economic and education stratification between neighborhoods exacerbated existing equity disparities within neighborhoods with high concentrations of poverty. Consequently, the recession hit those neighborhoods disproportionately harder, creating intense volatility in those particular markets. Declining incomes reduced people's ability to purchase homes, thus deflating prices in those neighborhoods. The findings around education and income may result from the disparities in wealth as it is "a powerful predictor of individual educational and economic outcomes, and despite their significantly lower homeownership ... the long-run consequences of these gaps are substantively important and difficult to overcome."[vi]

But how does the concentration of blackness impact demand among all buyers – whether from the community or not? Income and education certainly matter, but how much of the demand that impacts housing price is affected by how people around it are perceived? In other words, what is the cost of racial bias?

Real estate agents have been shown to direct black and white home buyers differently based on racial stereotypes, reinforcing patterns of racial segregation. Researcher Sun Jung Oh and John Yinger reviewed four different national studies on the topic in a 2015 article and found a common thread: There is "evidence of statistically significant discrimination against home seekers who belong to a historically disadvantaged racial or ethnic group."[vii]

Some of this research is not about devaluation, per se, but about steering and price discrimination. It indicates that blacks actually pay more than whites for equivalent housing. The focus of our research and my submitted testimony today is on how lower prices in majority-black neighborhoods convey lower value.

In U.S. metropolitan areas, 10 percent of neighborhoods are majority black, and they are home to 41 percent of the black population living in metropolitan areas and 37 percent of the U.S. black population.

Black Americans are highly urbanized. 90 percent live in metropolitan areas, compared to 86 percent of all U.S. residents. And decades after the Civil Rights movement, blacks remain highly segregated. Though blacks comprise just 12 percent of the U.S. population, 70 percent live in neighborhoods that are over 20 percent black, and 41 percent live in majority black neighborhoods. These majority black neighborhoods may be overlooked as sites for economic development, but they contain important assets, in terms of people, public infrastructure, and wealth.

Majority black neighborhoods in metropolitan areas are also home to 14.4 million non-Hispanic black residents and 5 million residents from other racial and ethnic groups. They also house a large portion of the nation's human capital, in that 2.3 million adults 25 and older call majority black neighborhoods their home, representing 5 percent of the nation's metropolitan population with a bachelor's degree, and 10 percent of its public schools and 6 percent of its libraries.

There is also wealth in these neighborhoods. In metropolitan America, there are 3.2 million owner-occupied homes in majority black neighborhoods, 5 percent of the total, and they are collectively worth $609 billion.[viii] Likewise, over 3 million business establishments are located in majority black metropolitan neighborhoods, 7 percent of all metropolitan businesses.

In the average U.S. metropolitan area, homes in neighborhoods where the share of the population is 50 percent black are valued at roughly half the price as homes in neighborhoods with no black residents.

Across metropolitan America, housing prices are systematically lower where neighborhood black population share is higher. In neighborhoods where less than 1 percent of the population is black (which we refer to as "non-black neighborhoods"), median listing prices on Zillow are $341,000 compared to $184,000 in majority black neighborhoods. Using Census Bureau estimates from homeowners yield similar discrepancies. Comparing only homes within the same metropolitan area, both data sources suggest that home values are just over 50 percent lower in neighborhoods where the black population is 50 percent compared to neighborhoods with no black residents.

The devaluation of black neighborhoods is widespread across the country. There are 119 metropolitan areas with at least one majority black census tract and one census tract that is less than 1 percent black. In 117 of these 119 metro areas, homes in majority black neighborhoods are valued lower than homes in neighborhoods where blacks are less than 1 percent of the population. Gainesville, Fla. and Sebring, Fla. are the only exceptions.

TABLE 2

The 10 metropolitan areas with the largest and smallest differences in the value of homes

Black neighborhoods in U.S. metropolitan areas, 2012-2016

	Median value of homes in majority black neighborhoods	Median value of homes in neighborhoods with less than 1% black population	Relative valuation of black neighborhoods in percentage points
Areas with the largest difference in home value			
Bridgeport-Stamford-Norwalk, CT	$131,011	$783,887	17%
Charleston-North Charleston, SC	$130,854	$717,711	18%
Savannah, GA	$112,539	$562,500	20%
Hilton Head Island-Bluffton-Beaufort, SC	$93,262	$460,712	20%
Youngstown-Warren-Boardman, OH-PA	$33,045	$131,484	25%
Port St. Lucie, FL	$65,880	$259,926	25%
Palm Bay-Melbourne-Titusville, FL	$61,662	$241,853	25%
Lexington-Fayette, KY	$77,270	$301,526	26%
Cape Coral-Fort Myers, FL	$67,192	$259,118	26%
Ann Arbor, MI	$68,320	$259,985	26%
Mean of group	**$84,104**	**$397,870**	**21%**
Areas with the smallest difference in home value			
Greenville-Anderson-Mauldin, SC	$82,680	$114,743	72%
New York-Newark-Jersey City, NY-NJ-PA	$403,314	$559,706	72%
Baton Rouge, LA	$109,951	$152,543	72%
Boston-Cambridge-Newton, MA-NH	$313,353	$430,997	73%
Naples-Immokalee-Marco Island, FL	$390,200	$459,728	85%
Asheville, NC	$178,200	$195,882	91%
Lakeland-Winter Haven, FL	$82,559	$89,334	92%
Anniston-Oxford-Jacksonville, AL	$59,371	$61,200	97%
Gainesville, FL	$95,591	$95,237	100%
Sebring, FL	$134,600	$69,644	193%
Mean of group	**$184,982**	**$222,901**	**83%**

Note: Sample limited to metropolitan areas with at least one census tract that is majority black and at least one census tract that is less than one percent black.
Source: Authors' analysis of 2016 American Community Survey 5-year estimates

The valuation gaps are extreme in a number of areas. The largest gap is in the Bridgeport-Stamford-Norwalk, Conn. metropolitan area. In neighborhoods where blacks are less than 1 percent of the population, the median home value is $784,000, compared to just $131,000 in majority black neighborhoods, a six-fold difference. Home values in majority black neighborhoods are just 17 percent of those in non-black neighborhoods. Likewise, very large differences are found throughout the South and Midwest—in Charleston, S.C., Cape Coral, Fla., Youngtown, Ohio, and Ann Arbor, Mich.

There is nonetheless an extremely wide range of estimates across metropolitan areas for the housing market penalty for homes in black neighborhoods. In the New York City metropolitan area, median home values in majority black neighborhoods are over $400,000, reflecting the extraordinarily high overall cost of living and value of real estate. That is much less than the value for neighborhoods with fewer than 1 percent black population shares ($560,000), but the percentage point gap is much lower than other parts of the country. Greenville, S.C., Boston, Mass., and Baton Rouge, La. are other examples of metro areas with relatively narrow gaps in valuations between majority black neighborhoods and those with few black residents.

Neighborhood quality is only part of the explanation for the devaluation of homes in black neighborhoods.

During the 20th century, segregation and Jim Crow forcibly lowered the quality of neighborhood conditions for blacks and impeded their financial ability to move to better opportunities. This occurred through deed restrictions, redlining, and zoning, as well as other mechanisms. As a result of that dynamic and the continuation of housing policies that exclude working-class housing from non-black neighborhoods, majority black neighborhoods suffer from lower quality housing and limited access to good schools and neighborhood amenities.

TABLE 4

Neighborhood characteristics by black population share

U.S. metropolitan areas, 2012-2016

Black population share	School test scores (Standardized)	EPA Walkability Index	Number of restaurants	Number of gas stations	Percent who use public transportation	Average commute time (minutes)
0%-1%	0.29	-0.31	53.2	6.9	3.6	26.7
1%-5%	0.28	-0.03	69.3	8.1	5.1	26.5
5%-10%	0.17	-0.01	69.7	9.2	4.7	26.6
10%-20%	-0.01	-0.01	67.5	10.0	5.4	26.5
20%-50%	-0.27	0.01	61.9	10.6	7.7	27.1
50% or higher	-0.85	0.23	50.0	10.8	15.0	29.2

Source: Authors' analysis data from 2016 American Community Survey 5-year estimates, Department of Education, Environmental Protection Agency, and County Business Patterns

The quality of housing in majority black neighborhoods differs from less black neighborhoods in terms of age, size, and structure. The median home in majority black neighborhoods is 12 years older than homes in neighborhoods where blacks are less than 1 percent of the population. These older homes are also smaller, by nearly half a room, and are much less likely to be detached single-family homes. Majority black neighborhoods are much more likely to have denser housing structures, such as attached single-family units, which also reflects the concentration of blacks in America's cities.

Not only is the housing stock of lower quality, so is the surrounding neighborhood in several important dimensions. School performance is weaker, commute times are longer, and access to business amenities is more limited. There is also evidence that exposure to environmental pollution is greater, through, for example, proximity to a greater number of gas stations.[ix]

The school test score gaps between neighborhoods are particularly extreme. The gap in test scores between majority black neighborhoods and those that have black population shares that are 5 percent or lower is approximately 1.1 standard deviations. More concretely, the proficiency rate on state exams in majority black neighborhoods is only 15 percent, compared to 60 percent in neighborhoods with less than 1 percent black population shares.

Likewise, residents of majority black neighborhoods confront longer commute times by several minutes compared to those in other neighborhoods, suggesting constrained access to jobs. Yet this interpretation requires caution because residents of majority black neighborhoods are far more likely to commute via public transportation, which can be slower, especially via bus.

Still, the apparent weaknesses of black neighborhoods can also be strengths. With homes more densely situated, residents of black neighborhoods live in more "walkable" communities, with a greater diversity of business types and more frequent intersections. These qualities are associated with higher home values.[x] There is a striking difference, on this score, between majority black neighborhoods and neighborhoods that are less than 1 percent black; they differ by over half a standard deviation.

Given the above discussion of housing and neighborhood attributes, the central question of this study remains: Do the differences in housing and neighborhood quality fully account for the differences in housing values?

Our analysis suggests not. My colleagues and I used a regression analysis to predict home values as a function of the black population share, the qualities of homes in the neighborhood, and the qualities of the neighborhoods within each metropolitan area.

First, there is clear evidence that adjusting for the size of the home lowers the devaluation estimate for black neighborhoods by a meaningful fraction—from -51 percent to -35 percent when we use the two Zillow-based measures for median list price overall and by square foot. Since, black homes are smaller, they have less market value, but that still leaves a very large gap unexplained.

The value metrics that do not include square footage are sensitive to the structural features of homes in the neighborhood—such as age, number of rooms, percentage detached, but adjusting these things did not greatly reduce the devaluation estimate. The Zillow median list price estimates for devaluation in neighborhoods that are 50 percent black range from -40 percent to -44 percent, with census-based estimates from owner self-appraisals in the middle at -41 percent.

The next set of regression estimates included neighborhood control variables, and these variables go further in explaining the devaluation of majority black neighborhoods. The devaluation estimates are -22 percent for median list price and -23 percent for the list price per square foot and self-appraisals of all owner-occupied properties.

In the model that predicts value per square foot, three variables measured at the neighborhood level stand out as strong predictors: school quality—measured by state test scores (strongly positive); the number of gas stations (strongly negative) and access to public transportation (strongly positive). Majority black neighborhoods are at a disadvantage on school quality and exposure to gas stations but have greater access to public transportation. Walkability predicts modestly higher home values, and black neighborhoods have an advantage on that score as well.

While our analysis explains roughly half of the devaluation effect, we are left with the fact that a square foot of residential real-estate is worth 23 percent less in neighborhoods where half the population is black compared to neighborhood with few or no black residents, even after adjusting for housing quality and neighborhood quality.

To put this devaluation value in perspective, we estimate that home values in majority black neighborhoods should be worth an additional $48,000 per home, which amounts to a cumulative sum of $156 billion in aggregate value.[xi]

With more effort or with local knowledge, sophisticated shoppers can also find out information about school quality, using the same data included in our models, test proficiency rates. There are no publicly available metrics on school quality available to consumers beyond what was included in our model. With further effort or by exploring the neighborhood, potential buyers can also get a sense of access to restaurants, libraries, and other business amenities. Our model used measures for these amenities that best explain variation in housing, without regard to how inclusion of these variables affected the estimate for devaluation associated with black population shares. We also adjusted for the length of commute and the mode of commute and several variables that capture neighborhood household age and family relationships.

Metropolitan areas with greater devaluation of black neighborhoods are more segregated and produce less upward mobility for the black children who grow up in those communities.

Black males earn lower incomes as adults than white males, even when born to parents with similar incomes. In this sense, blacks have lower intergenerational mobility than whites—as well as Hispanics and Asians. Intriguingly, this is not true for black females, who have similar incomes as white females born to parents at the same income scale. These finding comes from recent research by Harvard economists Raj Chetty and Nathaniel Hendren—along with Census Bureau economists—which linked records from the Internal Revenue Service to the Census Bureau to understand intergenerational income mobility for people aged 31 to 37 who were born between 1978 and 1983.[xii]

We used these data to investigate whether or not black children raised in areas with greater devaluation of black assets experience less mobility. There are several reasons why this might be so. There are large gaps in wealth between races and residential real estate wealth is a major reason for this gap.[xiii] If properties in black neighborhoods were priced equally as those in white neighborhoods, black children coming of age in the 1990s and 2000s would have had much more wealth to draw upon to pay for things like private schooling, tutoring, travel, and educational experiences, as well as higher education and greater access to higher scoring schools in the suburbs. Greater property wealth may have also facilitated higher rates of entrepreneurship among black parents, which may have positively affected children.

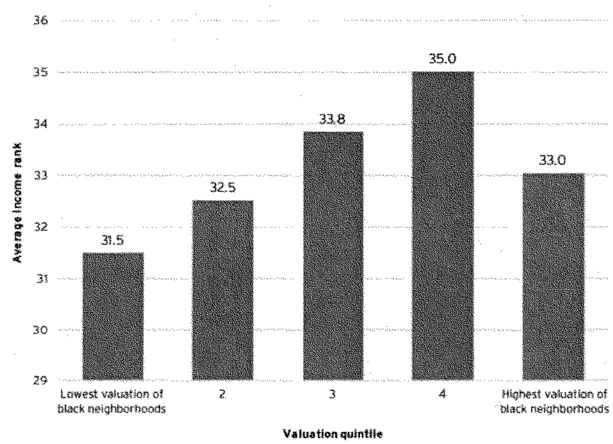
In fact, there is a positive correlation between the valuation of properties in black neighborhoods and upward mobility of black children whose parents had incomes at the 25th percent of the national income distribution. In other words, black children born to low-income families had higher income as adults if they grew up in a metro area that valued black property closer to its observable market characteristics. We restrict this analysis to the 113 metropolitan areas with at least one majority black neighborhood. We also gave extra weight in the analysis to metro areas with larger black populations to reduce the influence of measurement error; as such, the estimates should be thought of as characterizing the experience of the average black person living in different types of metropolitan areas.[xiv]

As shown in the figure below, metropolitan areas in the lowest quintile of valuation for majority black neighborhoods compared to white neighborhoods generate very low upward mobility for black children born near 1980. The average black child born in these areas to families at the 25th percentile of the national income distribution advances only to the 31st percentile. In areas with greater valuation for black neighborhoods, in the fourth quintile in particular, children end up in the 35th percentile. The positive relationship is more muted for the areas with the highest valuations of black neighborhoods.

FIGURE 2

Effect of housing valuation on upward income mobility of black children

Majority-black neighborhoods in U.S. metro areas, 2012-2016



Note: Income rank calculated for black children born to parents at 25th percentile of national income. Devaluation measure is based on median list price per square foot after adjusting for home and neighborhood quality. Analysis is of 113 metropolitan areas with at least one majority black census tract and one tract with black population shares under 1 percent. Means are weighted by the number of black residents in metro area.
Source: Authors' analysis of data from Zillow, the 5-year 2016 American Community Survey and Equality of Opportunity Project. Devaluation measure is based on median list price per square foot after adjusting for home and neighborhood quality. Analysis is of 113 metropolitan areas with at least one majority black census tract and one tract with black population shares under 1 percent. Means are weighted by the number of black residents in metro area

The devaluation of majority-black neighborhoods is penalizing home owners in black neighborhoods by an average of $48,000 per home, amounting to $156 billion in cumulative losses. Over the years, segregation has negatively affected neighborhood conditions—fewer quality schools, in particular—and reduced the quality of homes by limiting access to finance. However, differences in home and neighborhood quality do not fully explain the lower prices. In addition, there are positive but overlooked assets in black communities like walkability of black neighborhoods and access to public transportation.

The finding that black children born into low-income families achieve higher incomes as adults if they grew up in metro areas where homes were less devalued is noteworthy and could be strengthened with further work that more directly links discrimination to barriers to mobility and explores the potential for neighborhood devaluation to serve as an active agent that worsens outcomes for blacks and their children.

The undervaluation of black assets in housing markets has other important social implications. Black homeowners realize lower wealth accumulation, which, among other effects, makes it more difficult to start and invest in business enterprises and afford college tuition for their children.

We hope to better identify some of the causes for this devaluation—including potential psychological mechanisms—in subsequent research. Some of the most enduring and pernicious effects of the more than 350 years of slavery, Jim Crow racism, as well as de jure and de facto segregation in the U.S., have been the internalization of stereotypes, insults, and dehumanizing innuendos about black people, stemming from the malevolent use of such tropes by the (white) people in power to justify discrimination—what researchers describe as unconscious bias. Our findings were generally consistent with the widespread presence of anti-black bias—whether unconscious or not, ingrained stereotypes and automatic associations of a particular group, and even outright discrimination and racism.

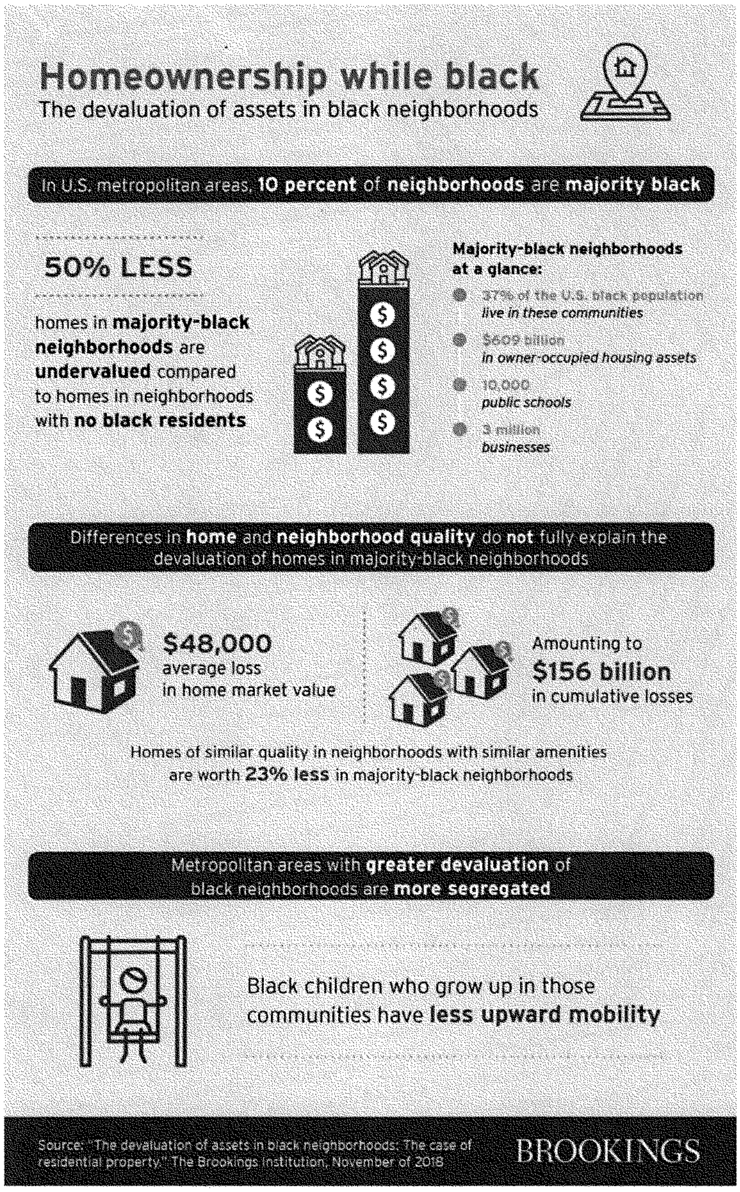
By controlling for commonly held causes of price differences including education, lower home quality, and crime, the work of myself and my colleagues suggests that bias is likely to be a large part of the unexplained devaluation of black neighborhoods and some perspective on how anti-black beliefs distort the value of assets. In the absence of representative survey data on racist beliefs at the metropolitan scale, we can't see the degree and nature of devaluation in the context of cities. Our future work aims to collect and analyze subjective survey data to see how people from different races view each other and their neighborhoods.

Chairwoman Clay, Ranking Member Duffy, Ranking Member Gooden,

Thank you again for inviting me to be here with you today. I look forward to addressing your questions and hope to work with you in the future.

The author would like to thank Jonathan Rothwell, David Harshbarger, and Anthony Fiano for their help in compiling this testimony.

The views expressed in these written remarks are those of the author alone and do not necessarily represent those of the staff, officers, or trustees of the Brookings Institution.


Homeownership while black
The devaluation of assets in black neighborhoods
In U.S. metropolitan areas, 10 percent of neighborhoods are majority black
50% LESS
homes in majority-black neighborhoods are undervalued compared to homes in neighborhoods with no black residents
Majority-black neighborhoods at a glance:
37% of the U.S. black population live in these communities
$609 billion in owner-occupied housing assets
10,000 public schools
3 million businesses
Differences in home and neighborhood quality do not fully explain the devaluation of homes in majority-black neighborhoods
$48,000 average loss in home market value
Amounting to $156 billion in cumulative losses
Homes of similar quality in neighborhoods with similar amenities are worth 23% less in majority-black neighborhoods
Metropolitan areas with greater devaluation of black neighborhoods are more segregated
Black children who grow up in those communities have less upward mobility
Source: "The devaluation of assets in black neighborhoods: The case of residential property," The Brookings Institution, November of 2018
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[iv] Caitlin Knowles Myers, "Discrimination and neighborhood effects: Understanding racial differentials in US housing prices." *Journal of Urban Economics* 56.2 (2004): 279-302.
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[vi] "Faber_Ellen_2016_Race_and_the_Housing_Cycle.Pdf," accessed October 3, 2018, https://wagner.nyu.edu/files/faculty/publications/Faber_Ellen_2016_Race_and_the_Housing_Cycle.pdf.
[vii] Sun Jung Oh and John Yinger, "What Have We Learned From Paired Testing in Housing Markets?," *Cityscape* 17, no. 3 (2015): 15–60.
[viii] This figure multiplies the median value of homes listed in black neighborhoods by the number of units. It likely understates the true aggregated value since the median excludes outliers.
[ix] Jean D. Brender, Juliana A. Maantay, and Jayajit Chakraborty, "Residential proximity to environmental hazards and adverse health outcomes." *American Journal of Public Health* 101.S1 (2011): S37-S52.
[x] Joe Cortright, "How Walkability Raises Home Values in U.S. Cities," CEOs for Cities (2009).
[xi] These figures rely on the Zillow listing price estimates. For Census-based estimates, we calculate a loss of $39,000 per home and $126 billion in aggregate. The calculation is done as follows: We take the log of median list price in majority black neighborhoods (the ln of $184,000 is .123) and add .23 (the devaluation estimate) and apply the exponential function, making make the value $232,000. The difference is our estimate of loss per home. We then multiply that by the number of homes in majority black metropolitan neighborhoods.
[xii] Raj Chetty, Nathaniel Hendren, Maggie R. Jones, and Sonya R. Porter. *Race and economic opportunity in the United States: An intergenerational perspective*. No. w24441. National Bureau of Economic Research, 2018.
[xiii] Thomas Shapiro Tatjana Meschede Sam Osoro, "The Roots of the Widening Racial Wealth Gap: Explaining the Black-White Economic Divide" (Institute on Assets and Social Policy, 2013), available at http://iasp.brandeis.edu/pdfs/2013/Roots_of_Widening_RWG.pdf
[xiv] A regression of our home and neighborhood quality adjusted devaluation measure (using Zillow list price per square foot) on upward mobility shows a coefficient of 0.02 and a t-statistic of 3.9, explaining .12 percent of the variation in a sample of the 113 metro areas with at least one majority black census tract and at least one non-black census tract (<1% black population). Limiting the analysis further to the 65 metro areas that are also among the 100 largest metropolitan areas by 2012–2016 ACS population, results in a t-stat of 4.1 and a r-squared of .20. Results are similar using the Census-based devaluation metric—again adjusted by quality.

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Testimony of Joan N. Trice
Before the Subcommittee on Housing, Community Development and Insurance
June 20, 2019

Chairwomen Waters, ranking member McHenry and members of the Subcommittee on Housing, Community Development and Insurance, thank you for the opportunity to share my thoughts regarding "What's Your Home Worth, a Review of the Appraisal Industry".

For most, buying a home is the largest investment they will ever make in their lifetime. There are many stakeholders who benefit from the consummation of a real estate transaction. The real estate appraiser is the only party to the transaction who is expressly unbiased and whose compensation is not contingent upon the deal.

An independent appraisal performed by a qualified licensed appraiser protects the lender from making risky loans and the homeowner from paying too much. The mortgage insurer relies upon credible appraisals to establish the LTV to calculate risk. Rating agencies need to accurately evaluate the underlying collateral values. Capital markets need transparency into the collateral valuation of each loan within the portfolio. All of these stakeholders rely upon a credible appraisal performed by a qualified licensed professional.

Most everyone here today likely read the book the Big Short or watched the movie, or both. I suggest you watch it one more time. Many of you likely assume we fixed all of those issues with Dodd Frank. I assure you, on the collateral side of the equation, we did not. In many ways it is in worse shape. Predatory appraisal practices are in full bloom. It feels very 2005ish to me.

The segment of the US population that suffers the most is the affordable housing sector when they pay too much for a home. To borrow a phrase from Josh Rosner, co-author of "Reckless Endangerment" a "home without equity is a rental with a mortgage". Current policies allow appraised values to be "gamed". Seller concessions promote the practice of contract sales prices to be inflated. This policy and the resulting compounding effect by its very nature makes affordable housing no longer affordable. Truth in valuation should be a right of every homeowner. Just remember one thing if nothing else that I state here today--"Value is not negotiable. Sales prices are." Appraisers, by and large, are not appraising properties too low. Properties are selling for inflated prices. Please examine carefully these policies.

These inflated sales prices subsequently become comparable sales that appraisers use in their next appraisal. These transactions feed automated underwriting engines and automated valuation models (AVMs). We must examine appraisal policies and practices, legislation, and guidance that prey upon the least sophisticated first-time home buyer. A rollback of the FRT exemption and resetting the de minimus threshold to zero would return to the original intent of FIRREA. Every transaction should require an appraisal to be performed by a licensed or certified appraiser.

I mentioned all of the stakeholders that the appraiser serves directly or indirectly. But who stands behind the interests of the appraiser? I respectfully submit that no one is. There is less transparency today than pre-Mortgage

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Crisis. For example, there has not been a single enforcement action against a lender for appraisal independence violations. Within Credit Risk Transfers (CRTs) the property address is not available preventing any due diligence on collateral valuations. This opaqueness forecloses on the concept of rational due diligence by the investor, who then must be wholly reliant upon an implied government guarantee.

I testified on November 16, 2016 that discussions about appraiser shortages, slow turn times, raising the de minumus threshold, FRT exemptions were all a ploy to "let's get rid of the appraiser". The Collateral Risk Network implores you to return to a focus of safety and soundness. A healthy vibrant market, a rational regulatory schema, and protections of appraisal independence with vigorous enforcement, will help cure all that ails the appraisal profession.

We've seen the tragic ending when a regulator (The FAA) leaves the regulated (Boeing) to self-regulate and audit themselves. This was done all in the name of expediency and regulatory relief. Fannie Mae and Freddie Mac are focused on modernization efforts that are not modern at all. Faster and cheaper should not come at the cost of safety and soundness. While Artificial Intelligence, Machine Learning, Big Data, and Blockchain technologies are all very exciting and will someday show great promise in advancements to the mortgage transaction, please be aware that much of what you hear is hype. Just like driverless cars, it sounds exciting, but we are decades away. Technology can augment the process making humans able to apply judgment to a highly complex decision.

First, we must have structural reforms and a regulatory schema in place (see attached regulatory diagram). Data standards and privacy rules need to be established. Who owns the data? Should the codified definition of market value be revisited? Should a public utility be established to maintain appraisal data and transfer rights to all of the stakeholders noted above? Should this data be made available to participants in the Common Securities Platform?

These are all challenging questions that must be thoughtfully considered. The data must be democratized and become transparent in order to maintain a safe and sound housing finance ecosystem.

The Collateral Risk Network, a group of chief appraisers and risk managers representing a broad spectrum of stakeholders, urges Congress to consider establishing a single consolidated authority to oversee the modernization of the valuation process. Much like the SEC provides oversight to a large and dynamic market, we envision a similar agency to fill the role in the housing finance markets. US residential real estate is the largest asset class in the world. It's imperative that we create a safe environment for all stakeholders.

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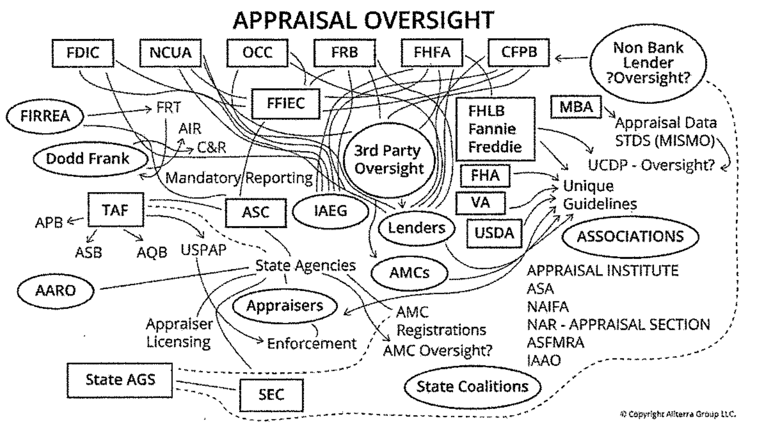


Modernization of the Appraisal System: A Regulatory Review

Introduction

On November 16, 2016, the Housing and Insurance
Subcommittee held a hearing on "Modernizing Appraisals: A Regulatory Review". Joan Trice, founder of the Collateral Risk Network (CRN) was invited to speak before that hearing.

As a result of that hearing, the Executive Council of the CRN met on January 29 through February 2, 2017 to discuss proposed structural reforms of the appraisal system to bolster oversight of collateral valuation and risk activities. The comments within this document contain a summary of our conversations.

Those in attendance included the following:
Joan Trice
Alan Hummel
Greg Stephens
Leland Trice
Ernie Durbin
Penny Reed
Michael Simmons
Crispin Bennett

Background

The Collateral Risk Network (CRN) is a group of over 500 chief appraisers, compliance officers and risk managers from lending institutions as well as appraisal management companies. The recommendations provided herein represent a consensus opinion among the CRN Executive Council. The CRN Executive Council is represented by Chairs and Vice-Chairs from various committees.

The guiding principles in the development of our recommendations, focus on what is best for the health, safety and welfare of real estate finance. Our mission is to ensure that collateral valuation and risk maintain a prominent role in the broader discussions of real estate finance reforms.

The real estate appraisal profession in the US was formed in the aftermath of the Great Depression during a challenging economic environment when high unemployment, default of 90% of mortgages, high rates of foreclosure and the subsequent failure of 15,000 banks. The real estate price bubble and collapse during this period was found to be caused by a real estate industry fraught with conflicts of interest, fraud and other types of abuse, particularly among professionals receiving commissions tied to the outcome of real estate transactions. As a result, the bedrock principle which led to the founding of the appraisal profession – is the principle of independence. The objective of the real estate appraiser industry is to insert a professionally trained expert, who is not part of the transaction and with no compensation tied to the outcome of the transaction, as a means to help protect the public, ensure the legitimacy and pricing of transactions and to reduce the rate of fraud, conflicts of interest and abuse.

Executive Summary

The CRN Executive Council proposes the establishment of a new agency that represents a consolidation of the Appraisal Subcommittee (ASC) and the Appraisal Foundation (TAF). The goal is to simplify, streamline, strengthen and modernize the appraisal system to preserve safety and soundness in real estate finance. In addition to those functions currently managed within the ASC and the TAF, all real property valuation policy, regulation, and oversight should be directed by this new entity to ensure cohesive protocols to protect the public trust.

This new authority, the Collateral Risk Agency (CRA), would safeguard appraisal independence, transparency, and integrity in the collateral valuation process to enable proper and cohesive risk management for the largest asset class in the United States.

The historic mortgage crisis that crippled the US economy occurred due to the simple reality that profit motivation eventually supercedes risk management. The recent decisions by Fannie Mae and Freddie Mac to expand the valuation waiver policy, is another example of short memories and an example of removing prudent policy in order to expand loan production and profitability.

Simplify- Collateral valuation has experienced systemic failure as evidenced during the mortgage crisis. Subsequently, several modifications were made, most notably Dodd-Frank, that only anemically altered behaviors. The CRA is not a proposal to expand regulation but to consolidate several disjointed agencies into one unified entity. The CRA would oversee all valuation of real estate.

Streamline- By consolidation of what today is inconsistent, conflicting and often indecipherable policy, the "rules of engagement" become clearer and compliance less costly for all stakeholders.

Modernize- US real estate and all of its derivative products is the largest asset class in the world yet we know little about it. It is time to modernize one of the pillars of the real estate economy, collateral valuation and risk. Data standards must be set and systems constructed to ensure a scalable, secure infrastructure.

Strengthen- Oversight of appraisal practices becomes more effective when the rules are clear. Constant monitoring of appraisal reports, screening of participants, and monitoring of market trends will promote safe and sound lending activities as well as ensure the public trust.

The CRA would be responsible for:

1) Establishing a federal appraiser licensing program with disciplinary handled at the state level
    a. Education guidelines and approvals
    b. Fund state disciplinary and peer review programs
    c. Minimum licensing standards
    d. Practice, procedures, policy
    e. Ethics
    f. Defining value definitions
2) Data & Technology
    a. Data standards
    b. Unique identifier for appraisers, AMCs, and all real estate
    c. Registration of all participants and maintenance of a registry
3) Oversight & Enforcement
    a. Monitor appraisers, AMCs, lender appraisal programs, and subscribers to repository
    b. Impose fines and deny access to repository to fraudsters and/or incompetent appraisers or AMCs.
    c. Oversee the activities of a repository of all valuations and subscribers

Current State

<u>The Appraisal Subcommittee</u>

The Appraisal Subcommittee of the Federal Financial Institutions Examination Council (FFIEC) was established in August 1989 pursuant to Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act. Title XI's purpose is to "provide that Federal financial and public policy interests in real estate transactions will be protected by requiring that real estate appraisals utilized in connection with federally related transactions are performed in writing, in accordance with uniform standards, by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision."

The FFIEC is responsible for oversight of appraisal activities within housing finance. The Consumer Finance Protection Bureau (CFPB) seems to have little oversight of the nonbank lenders' appraisal activities. The other agencies have no bank examiners on staff who are appraisers. This was not true several decades ago. There are some large national banks who do not have a chief appraiser. The last appraiser on staff with a FFIEC agency retired a few months ago. The FFIEC, by its very nature, has not been responsive to writing final rules as mandated by Dodd- Frank.

Systematically the rules have been relaxed surrounding appraisal issues by raising the transaction threshold and modifying the definition of a Federally Related Transaction (FRT) to exempt approximately 95% of transactions, which nullifies the intent of FIRREA. Given that "safety and soundness" is the mission of the FFIEC, these actions are incomprehensible.

State Oversight of Appraisers

The existing appraisal regulatory structure involves licensing of appraisers at the state level. Most states do not have an independent appraisal agency. Many fall under a Real Estate Commission while others fall under a general licensing bureau that may include cosmetologists, barbers, and undertakers and so on. Some state agencies' have their funds swept into a general fund. Most states do not have someone with an appraisal background heading up the appraisal agency.

Each state has a unique renewal process. An appraiser in the Mid Atlantic, for example, will find that their Delaware license renewal period does not coincide with their Maryland renewal cycle causing them to take duplicative continuing education courses. If you are a commercial appraiser doing business in multiple states, you can apply for a temporary license. The application and approval process can take months causing the opportunity to be lost. If the property is a specialty type property, finding a local appraiser is often not an option, leaving the lender and the borrower at a disadvantage.

Many states pass legislation that is more restrictive than the policies implemented by the Appraisal Subcommittee (ASC). For example, some states require that a review appraiser be licensed in the state where the property is located. This requirement imposed upon a national lender would require them to hire reviewers in each state or require them to maintain multiple licenses. And then of course, there is a jurisdictional question. Can the Arizona state appraisal agency act against an appraiser in California? There is no restriction imposed by federal banking regulators. The guidance is simply to abide by state laws.

While real estate is local, lending is national, and in many cases, global. We have an appraisal regulatory structure that has not kept pace with the changes in housing finance over the past several decades. The maze created by state and federal agencies create conflicts and lack of accountability. Many of the rules within Title XIV of Dodd- Frank have remained unenforced or unenforceable. The weaknesses magnified during the housing finance crisis have yet to be cured. Risks to the housing finance system created by a complicated structure are the subject of frequent CRN Executive Council discussions. Structural reforms must include appraisal reform issues to restore safety and soundness to the housing finance system.

The Role of the Appraisal Foundation

The Appraisal Foundation (TAF) is a non-profit organization established in 1987. TAF maintains the Uniform Standards of Professional Appraisal Practice (USPAP). Appraisers are required to take a 7 hour USPAP course every two years. TAF modifies USPAP every two years to mandate course renewals and fees. Approximately 80% of the TAF budget is derived from the sale of USPAP courses. Unfortunately, this misaligned incentive may be one of the primary reasons the document increases in complexity. The appraisal community and stakeholders would be better served if this document was published in a more dynamic environment.

The USPAP book is 378 pages long. It is a highly complex document that, according to a recent survey by Appraisal Buzz, is not understood by 60% of appraisers. That is an astounding failure. Following basic standards and ethics should not be that complex. USPAP should be free and readily available and on the corner of every stakeholder's desk.

Appraisal courses are approved at both the Appraisal Foundation level and at the state level requiring course providers to pay multiple fees. Hosting a national appraisal conference requires applications to each of the states. This process is inefficient, stifles the development of new courses, and increases expenses to all stakeholders. While the Appraisal Foundation has a national course approval program only approximately half of the states accept it on a reciprocal basis while others charge an additional fee and require state submission for approval rendering any effort to standardize the continuing education process useless.

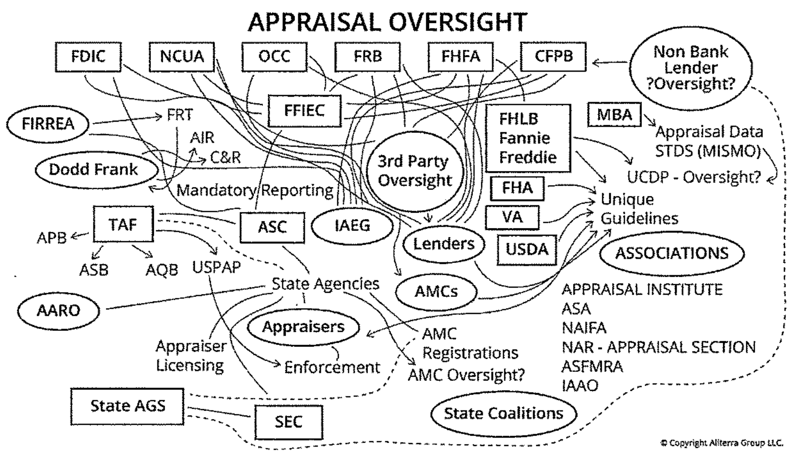
Fannie Mae and Freddie Mac guidelines sometimes collide with USPAP. USPAP fails to recognize a secondary market and hinders the ability for enforcement actions against bad actors. For example, due to confidentiality clauses in USPAP an appraiser cannot be held accountable by the investor. The GSE's certifications state the opposite. One of the many failures of our current regulatory system is the inability to remove bad actors from doing further harm. And during the period leading up to the mortgage crisis, bad actors actually flourished.

The stated mission of TAF is to ensure the public trust in the valuation profession. A pointed question was posed at the hearing... (paraphrasing) "what did TAF and ASC do in the years leading up to the mortgage crisis to stem the tide of appraisal fraud and overvaluation? And what has TAF or ASC done since"? The public trust in the appraisal profession is not in any better place today than during the housing crisis. While certainly overvaluation by appraisers was not by itself a catalyst for the mortgage meltdown it was assuredly a contributing factor. And while TAF was not solely responsible either, there are no records of proactivity by TAF defending appraisers from appraisal independence violations and protecting the public trust.

In summary, the current regulatory schema is confusing, with no central authority and no apparent accountability to any stakeholder. Few of the weaknesses identified and magnified during the housing finance crisis have been resolved. Dodd-Frank set up appraisal independence as its primary focus in Title XIV however there has been virtually no enforcement. It remains unclear with whom the enforcement authority falls.

We propose that FIRREA Title XI and Dodd-Frank Title XIV (appraisal sections) be repealed and replaced with a new law establishing the Collateral Risk Agency as the single authority for valuation. The modernization of the appraisal regulatory structure is long overdue. Continuing to operate with a legacy regulatory system is hampering a recovery that is genuine.

The diagram below is an illustration of our current regulatory structure:



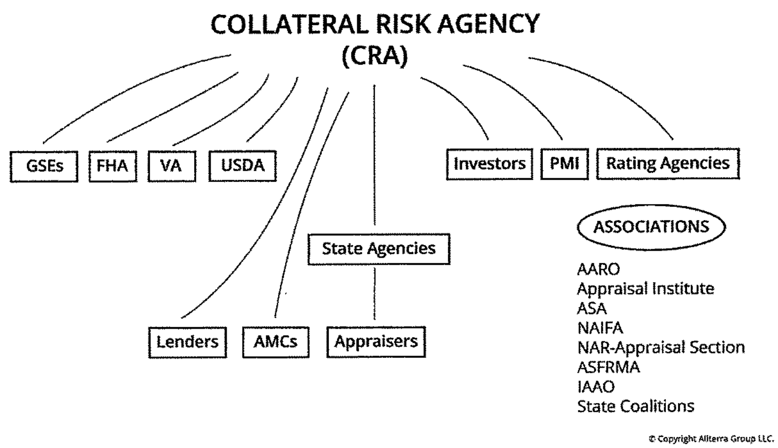
<u>Federally Related Transactions</u>
A report to the FFIEC by The Economic Growth and Recovery Paperwork and Recovery Act (EGRPRA) issued March 21, 2017 is a stunning example of the failures of our current regulatory structure. The EGRPRA report concludes that a federally related transaction (FRT) excludes transactions by Fannie Mae, Freddie Mac, USDA, the VA and FHA. This is absurd at face value. The threat of the banking agencies' actions cannot be overstated. Unless this interpretation is undone the oversight of 95% of the residential mortgage transactions are exempt from protections that an appraisal affords to the safety and soundness of the housing finance system. This appears to be a de facto unwinding of FIRREA, Title XI.

Another approach would be to rewrite the law to mandate that any transaction to be securitized on the secondary market must include an appraisal performed by a licensed or certified appraiser. These transactions would be regulated by the Collateral Risk Agency which would have purview over the valuation and collateral risk policies and activities of the GSEs, lenders, appraisers and other stakeholders.

More recently the GSEs have begun programs for appraisal waivers. It began with just rate and term refinances but has quickly devolved into waivers on purchases as well. These waiver programs, sanctioned by FHFA, appear to have no basis in safety and soundness, but merely marketing gimmicks in competition with each other in a "race to the bottom". This is reminiscent of waivers offered to WAMU and Countrywide during the early 2000s competitive death match. The GSEs should not be allowed to violate safety and soundness in exchange for sales goals. These are inherent conflicts of interest that their current regulator is enabling.

The inability of the appraisal community to garner any attention to the gap created by the FRT exemptions shines a bright light on the ineffectiveness of our current regulatory schema. A return to pre- FIRREA and pre- mortgage crisis practices is an open invitation for abuses and fraud where catastrophic losses were incurred, the very outcome Congress intended to avoid with the passing of Title XI and Title XIV. Bank regulators' collective amnesia suggest they should not be the caretakers of appraisal oversight.

The diagram below is an illustration of the proposed regulatory structure:



Structural Reform as a Single Authority

The CRN Executive Council unanimously agreed that the best solution to address the structural failures established by FIRREA would be a single regulator with authority over all valuation. Upon establishment of the Collateral Risk Agency (CRA) as the single authority, functions of the ASC and TAF would be merged under this single agency. The goal of the Collateral Risk Agency would not be to expand regulations but to merge and consolidate all valuation of real estate under one authority. This streamlines the regulatory system, allows for more effective oversight and expands the role of valuation in a more responsive manner to market demands.

The CRN Executive Council researched the Securities and Exchange Commission (SEC) as an applicable model to the CRA. The SEC was designed to have independent oversight of a critical financial market. In volume, the US real estate market and all of its derivative products is estimated to far exceed the equities market. The SEC manages standards, oversight, education and is responsible for preserving the public trust.

This new entity, the Collateral Risk Agency, will be responsible for:

- National qualifications and licensing program
- Education approvals
- Data standards and reporting standards and formats
- Data repository oversight
- Setting practice and procedures and ethics standards (a modernization of USPAP)
- Registration of AMCs, appraisers, and capital markets participants
- Oversight and enforcement of AMC activities
- Authority to impose suspensions of appraisers for high risk circumstances
- Examination and enforcement of lender appraisal practices and capital markets
- Establishing definitions of value

CRA's responsibilities would include oversight of all appraisal activities. All appraisal guidance, much of what is now issued by FFIEC, would become the role for the CRA. Having a single regulator for appraisal would remove the conflicts that occur between agencies. It would also provide a vehicle for responsiveness in dynamic markets. In historical models, the appraisal profession has experienced piecemeal legislation and guidance from a number of sources, many of them conflicting. The consolidation of valuation practice, policy and procedure under one authority with rational and consistent oversight would result in easing the burden of compliance.

Currently the ASC reports to the FFIEC yet that has proven to be an inverted regulatory structure. Generally speaking the FFIEC, comprised of six agencies, has been comprised of low level staff who have not been knowledgeable about appraisal matters. There is virtually no appraisal "brain trust" within these agencies who are tasked with oversight of appraisal activities at banks. Non-bank lenders appear to have no oversight at all with respect to appraisal activities. Given that approximately 80% of all lending is through the non-bank lender channel this inserts huge risks into the system. Oversight of the valuation functions with lenders should be the purview of the CRA.

There was vigorous debate as to where to situate this new entity. All agreed that for independence reasons, the entity should be free standing and not placed within an existing agency. Independence from the influences of loan production and political pressures are of utmost importance.

The structure of the CRA would model one similar to the Federal Reserve with a board of regional chief appraisers. We propose, in fact, that the regions mirror those set forth by the Federal Reserve. The Collateral Risk Agency would work closely with federal financial regulatory agencies and would share market data, and risk analytics. Risk alarms could be broadcast in real time to other regions. For example, if NYC is attracting foreign cash buyers that are money laundering schemes, this may create a bubble in certain sectors of a market. This appears to have also occurred in Miami almost simultaneously. New York state responded. FL has not. To the uninitiated, statistics might indicate that the Miami condo market has fully recovered. The statistics are deceiving. Risk alerts could be disseminated to real estate professionals, regulators, and to lenders and investors.

We discussed that leadership at the top would be a director, appointed by Congress to a 10 year term. Qualifications of the Director would include advanced degree and/or experience in economics, real estate, valuation, risk or finance. The Board of Chief Appraisers would be comprised of certified appraisers, past or present. The Board would be established by Presidential appointment and serve a term of 4 years (staggered), renewable terms not to exceed 14 years. Other key positions would be data and analytics and risk experts.

National Licensing

Congressman Douglas Barnard, during the crafting of Title XI of (FIRREA), originally intended for there to be a national appraiser licensing program. The "state's rights" argument prevailed which is one of the principle weaknesses in the current structure. Today, we have minimum standards established by the Appraisal Subcommittee and adopted by the states, not uniform standards. The result is that in addition to bank regulations, each state imposes their own set of rules. Insert GSE guidelines, unique VA and FHA guidelines and the impact upon the appraisal profession is an expanded scope of work that has rendered the appraisal process confusing at best, unenforceable for the most part, and allows fraud and incompetence to flourish at its worst. An appraisal should be uniform regardless which agency is involved in the financing.

Create a national license program but with state oversight of discipline. Each state should maintain peer reviews of licensee work product to bring the appraiser along in their professional development. We currently have a system of punishment rather than a more constructive approach. If a state fails to act in a responsive manner to criminal or risky behavior by the licensee, the CRA should have the authority to suspend the licensee pending adjudication. States that adopt the federal standards would receive funding for their oversight functions.

The Collateral Risk Agency would oversee a federal registry of all appraisers' credentials and disciplinary records. Each appraiser would be assigned a unique identifier. It should be noted that the CRA would be responsible for establishing minimum criteria for licensing but would not relieve either the lender or their third parties from performing their own due diligence and fitness of the appraiser for a assignment.

AMC Registration and Oversight

Appraisal Management Companies (AMCs), third parties, flourished with the establishment of HVCC and consequently the passing of Dodd-Frank. Lenders (especially nonbank lenders) engage AMCs as a method to ensure independence from loan production. AMCs became the implicit safe harbor. The ASC was charged with creating a national registry of AMCs but the oversight of AMCs was to occur with state appraisal agencies.

This has essentially returned the appraisal process to an unregulated area, placing housing finance at risk. Current estimates are that 80% of valuations flow through an AMC. States are ill prepared to monitor the oversight of national companies. Requiring AMCs to register with each state individually creates an undue burden on AMCs to comply with unique state licensing laws. This adds inefficiencies and expense for no meaningful purpose. AMCs should be registered at the federal level and would be within the purview of the CRA.

The CRA would annually audit AMCs and have the authority to randomly spot check based upon complaints or indications of risky behavior. Site visits would be required periodically. AMCs would be monitored for adherence to appraisal independence to ensure loan production plays no role in the appraisal process. This can be done by a review of each client, loan volume, loan originator for each file and assignment of an appraiser for each order. Each "actor" would be assigned a unique identifier so that imbalanced relationships can be monitored. An audit of the AMC panel would assist in the discovery of a bad actor who is potentially abusing the system.

No lender, bank or non- bank, would be allowed to own their own AMC. If a bank or a non-bank lender is too small to separate loan production from appraiser selection, an AMC would be required to establish a firewall to maintain appraiser independence. The CRA would monitor assignments and require certifications that no one in loan production can influence the selection of the appraiser by nomination to a panel, referral, or placement for an order. All conflicts of interest would be monitored. For example, some mortgage brokers have their family members establish an AMC and have used LLCs to obfuscate true ownership. This activity would be concerned fraudulent and would be enforced. The CRA would monitor the blind ordering processes of appraisal transaction platforms to ensure independence.

One of the components of Dodd-Frank was the Customary & Reasonable fee provision. This has never been enforced due to an interim final rule written by the Federal Reserve which contradicted the law. This has left confusion in the marketplace. The simple approach would be a repeal of the interim final rule on C&R. The modification to the rule would require the lender to pay for the services of any third party they engage. The law should be amended to require that the fee collected by the lender be the fee paid to the appraiser and duly transparent and reported. These fees would be established by market studies of fees by government agencies or independent private sector fees surveys, or lender fees paid (in the absence of a third party). The lender would then, just as they do with other vendors, issue a Request for Proposal (RFP) and respond to competitive bids. This would remove the misaligned incentive for an AMC to engage the cheapest appraiser, not the best appraiser. This would encourage use of technology to enhance efficiencies, promote quality appraisal reports, and more accurately inform the consumer of the true cost of the appraisal process.

A lender must maintain an appraisal department that is entirely independent of loan production or they may engage third parties or a combination of both. The lender must choose a path that serves their risk management best practices. The practices, policies and procedures of the lenders and their third parties will be overseen by the CRA.

Data & Technology

Appraisal forms, which drive the appraisal process are the domain of Fannie Mae and Freddie Mac. VA and the FHA adopt these forms as their own and add additional addenda. In the 1960s these forms were the domain of the Savings & Loan League and were co-opted by the GSEs sometime during the 1970's. As a result, the forms have not been updated to accommodate legacy systems internal to the GSEs. The GSEs, rather than adopting the MISMO standard, created their own standard. In order for the GSEs to modernize appraisal forms they would have to scrap UCDP and start over. While there are over 300 data points contained with the residential report only 23 are currently accepted into the Uniform Collateral Data Portal (UCDP). In short, UCDP was outmoded the day it launched because they did not take the time to create a "data centric" system. They instead created a "form centric" database.

UCDP was established post mortgage crisis as a result of the HVCC agreement between the NYAG, FHFA and the GSEs. Within that agreement was a $24 million penalty to be imposed upon the GSEs and to be used to establish the Independent Valuation Protection Institute (IVPI). The details of the IVPI were never defined. By mutual agreement between the NYAG and the FHFA, these monies allocated for IVPI, were used to establish a repository of appraisal data instead.

The original plan for UCDP was for each stakeholder to be afforded access to this repository based upon access rights and permissions. The stakeholders included:

Lenders
AMCs
Servicers
Investors
Appraisers
Rating agencies
Private mortgage insurers
Regulators
Government agencies

The original plan for UCDP was never executed. Complaints by many stakeholders are that Fannie Mae and Freddie Mac have a monopoly on the data. As intended, the property information and valuations are not ending up as a part of the securitization offering. Mortgage backed securities today still do not benefit from transparency into the underlying valuation or risk metrics. Our proposal is that a 501(C) 3 is established to create the public utility of a data repository of appraisals, real property registry, and registry of all real estate participants.

Revenue from this repository would ensure that the CRA remains financially self-funded. There would be a registration fee required to be a recipient of the data. Additionally, transaction fees would be instituted to ensure that the database is dependable and secure. The purpose of the repository would be to promote safety and soundness of the appraisal process through transparency. This data will be leveraged for appropriate collateral risk analysis.

Today one of the weaknesses of the UCDP is that the GSEs have no mechanism to verify data or reconcile conflicting data. Fannie and Freddie have no "hard stops" at the gateway. Known bad actors should not be allowed to deposit appraisal reports into a data repository. Access to better data will make collateral risk decisioning a science for the next generation of housing finance.

CRA would develop new reporting formats to accommodate a less stringent format than today's "one size fits all" forms. The reporting format would be predicated upon the risk profile of the collateral and its market. Data standards have already been established with MISMO. There are other standards that have never been established. For example, the square footage of a home would seem to be one that was well established, yet it is not. The GSEs have never set a standard on how to measure a home yet they score appraisers against their peers for square footage. The square footage of a home should become fact based and not malleable depending upon regional differences.

The collection of and access to standardized reliable data will be revolutionary. It is astounding, given that US real estate and all of its derivative loan products, is the largest asset class in the world, yet we know little about the underlying collateral. Establishing a unique identifier, cataloging each parcel and improvements, and establishing data standards will promote responsible lending and investing. Appraisal data is a critical component of the broader "real estate super highway". This is the foundation necessary to create a scalable housing finance system.

Policy, Practice and Procedure

One of the ongoing debates within housing finance has been surrounding the role of the appraiser- who must perform one, when is one done, and fundamental questions such as what is an appraisal. FIRREA established licensing of appraisers and mandated that each "federally related transaction" or FRT required an appraisal by a licensed or certified appraiser. Later exemptions were added, transaction thresholds increased, and evaluations introduced to allow for valuations to be performed by real estate agents and unlicensed or unregulated parties.

In a new regulatory schema, there should be unequivocal boundaries that limit valuations to be performed by licensed individuals only, appraisers, subject to regulatory oversight. This is essential to provide safety and soundness to housing finance.

The definition of market value was defined in FIRREA. The definition is flawed. A lot of blame has been placed upon appraisers for failing to report credible values during the crisis. There is evidence once again that bubbles are forming in some overheated markets. The CRA would be charged with modifying the definition of market value. The definition should remain dynamic and should be the purview of the CRA to modify. The most likely model to emulate is the European one, "mortgage lending value", MLV. MLV is focused upon a sustainable value, with less emphasis on price which is subject to irrational behaviors by borrowers and irresponsible lending practices by lenders.

At present appraisal practices are driven by the requirements in the GSE's forms and their policies. Fannie Mae has become the de facto regulator and ultimate authority for appraisal practice. With the Collateral Risk Agency as the new authority the conflicting guidance would be unified into one cohesive set of rules. This new authority will be able to be responsive to the needs of the market and reactive to crises. The goal would be to moderate bubbles and avoid major catastrophic events as much as possible.

Science of Collateral Risk

With the aggregation of information, the CRA would provide market data to local appraisers as well as to investor analysts. Modeling could be developed at the zip code level and market segmentation. For example, analysis of the data may indicate that three bedroom homes in 21811 are increasing in value while four bedroom homes are not.

The CRA would proactively partner with universities that offer real estate programs to provide data for research and modeling. The CRA would also cooperate with other government agencies to offer access to data when appropriate.

Revenue

The CRA would be financially independent once the technology buildouts are completed. Registration fees of appraisers, AMCs and stakeholders who would be provided access to information. Transaction fees would be accessed upon upload and download. Registration fees would be assessed to stakeholders who would have access to the repository-rating agencies, investors, securitizers, lenders and private mortgage insurers. Estimates for revenue are as follows:

80,000 appraisers x $300=$24,000,000
500 AMCs x $5000= $2,500,000
7000 lenders, investors, PMI, rating agencies @ $20,000= $140,000,000
20,000,000 transactions @$10 each= $200,000,000

Based upon estimates to construct UCDP the cost to engage a technology provider to build the repository would be estimated at $50 million.

States would receive grants for maintaining a disciplinary program and peer review board provided they adopt the federal criteria, and do not expand the scope of the guidance. This would not be an unfunded mandate that exists in many states today. The unfunded mandates have caused some states to expand their roles to justify a layering effect of service fees. This has resulted in regulatory confusion and burdensome expense.

Conclusion

If the housing finance system is to move forward progressively and safely, solutions to the valuation component need to be put forth. It is the vision of the CRN Executive Council that the valuation component is but one segment of an overhaul of the broader housing finance reforms of regulatory structure as well as technical infrastructure.

Ultimately the "real estate superhighway" must be constructed for our housing finance to be scalable in a safe and sound manner. Appraisal data and information gathered during a site inspection would help establish and maintain a registry of every parcel of real estate and the improvements thereon. The investor market needs access to "point of origination" valuation information as well as "real time" data to properly access the risk of any given portfolio at any point in time. Every stakeholder benefits by the transparency afforded by a central repository of data. The CRA would provide oversight of the standards, methodology and access to this public utility.

In conclusion, the Collateral Risk Agency should be established an independent agency to be the custodian of the appraisal process. A holistic solution serving all stakeholders would set us on the right path for returning confidence in the markets for consumers, private mortgage insurers, rating agencies, lenders, home builders as well as investors.

Appraisal Institute®

Professionals Providing Real Estate Solutions

What's Your Home Worth? A Review of the Appraisal Industry

Testimony of Stephen S. Wagner, MAI, SRA, AI-GRS

2019 President

Appraisal Institute

Before the Subcommittee on Housing, Community Development and Insurance

House Committee on Financial Services

June 20, 2019

Chairman Clay, Ranking Member Duffy and members of the Subcommittee on Housing, Community Development and Insurance, thank you for the opportunity to testify on behalf of the largest professional association of real estate appraisers in the United States at today's hearing on "*What's Your Home Worth? A Review of the Appraisal Industry.*"

First, I will address the set of questions directed to us for today's hearing. Second, I will provide feedback on the two discussion draft bills relating to FHA appraisals and Appraisal Subcommittee registry fees. I will conclude with a set of recommendations for broader industry reforms we believe would be beneficial for consumers, users of appraisal services, and professional appraisers.

Question 1: Do you have concerns with the recent proposed regulation from the Federal financial institutions regulatory agencies to increase the de minimum threshold and ultimately increase the number of transactions that are exempt from appraisal requirements?

Yes, two pending proposals – one involving the federal bank regulatory agencies, and another involving the credit union regulator – would increase risk to safety and soundness of financial institutions and the health of the financial system. Specifically, the federal bank regulatory agencies have proposed to increase the residential appraisal threshold level from $250,000 to $400,000. This proposal does a complete "about face" from recommendations made by the same agencies in the Economic Growth and Paperwork Reduction Act (EGRPRA) Final Report delivered to Congress in 2017. In 2017, the agencies opted not to increase the residential appraisal threshold level based on safety and soundness concerns and additional worries about losing consumer protections. Today, the agencies are about to turn their backs on the EGRPRA final report purely to promote regulatory relief, even with 90+ percent of commenters writing in opposition to the proposal to increase the residential appraisal threshold level to $400,000. In the interim, Congress enacted a discrete regulatory relief provision with S. 2155 for rural residential loan situations. This provision has simply not been given an opportunity to be implemented by regulated institutions.

Real estate appraisal is a highly regulated profession. As an appraisal practitioner, I deal with a multitude of rules and regulations with nearly every aspect of my practice. My experience also includes working within a bank managing residential and commercial appraisal operations. I understand concerns about and the need for regulatory relief in the financial sector. However, we must not ignore the need and benefits of regulation. At the heart of the financial crisis was a minimization of risk management activities – including appraisal functions – throughout the real estate financial sector. We cannot allow the regulatory relief pendulum to swing too far the other way, and in doing so, sow the seeds for the next financial crisis.

This is where we are today with appraisal requirements. We are fast moving to *optionality* in appraisal. The very definition of "de minimis" is one too trivial or small to merit consideration. The de minimis appraisal threshold levels are now proposed to represent most transactions. This represents a complete reversal of Congress' intent when it enacted FIRREA in 1989.

This is witnessed today by the proposal by the National Credit Union Administration to increase the nonresidential appraisal threshold level from $250,000 to $1 million. If this proposal is finalized, as we understand the agency was recently preparing to do, it will likely result in the federal bank regulators having to reissue their now final rule establishing a $500,000 commercial real estate appraisal threshold level. The federal bank regulatory agencies would likely feel compelled to increase the threshold to $1 million simply to level the playing field between banks and credit unions in reduced appraisal requirements. Because of this, the agencies are competing over which sector of the financial community can do the least due diligence. Frankly, this is preposterous and should be a concern to all taxpayers, who ultimately pay the bills for failures in our financial system.

Question 2: Are there ongoing concerns that appraiser independence is being undermined, and if so, what more can Congress do to strengthen appraiser independence protections?

Yes, ultimately, the attempts to increase appraisal threshold levels will cause a reduction in appraiser and appraisal independence, as they represent a dramatic <u>deemphasis</u> on risk management activities within regulated financial institutions. As the appraisal threshold level increases, the number of loans eligible for evaluation allowances increases with it. Evaluations can be prepared by internal bank staff and those who carry no ethics or standards obligations, unlike appraisers. The lines of separation within financial institutions quickly devolve and become murky. Through the last two real estate related financial crises, we have experienced loan production operations gradually exert pressure on risk management functions like appraisal – when left unchecked, and we would expect this to occur should these two proposals be finalized.

Overt "value pressure" – or pressure to deliver inflated appraisals to satisfy those with vested interests in the transaction is likely less common today, largely because mortgage brokers have been removed from the appraisal ordering process. This was a major problem during the lead up to the financial crisis. Sometimes we hear the opposite scenario, where appraisers have been asked to lower the appraised value in reaction to support for things like green or energy efficient features.

Appraisers experience pressure in less overt or masked ways from any number of parties to the transaction, including:

- Negotiated service matters such as turnaround times. We must be careful not to emphasize these and other factors that detract from the quality of such services. Nobody benefits from a professional service that cuts corners or is so watered-down that it loses reliability or credibility.
- Use of Reconsiderations of Value on a frequent basis. Unless appraisers have clearly missed pertinent data to the appraisal at hand, reconsiderations are often a waste of time and resources.
- Use of Borrower Estimates. These may be communicated orally by someone working with an appraisal management company, or even delivered on forms provided to the appraiser by lenders.
- Denying access to the property to steer the appraisal assignment to a favored appraiser.
- Providing erroneous information and submission of incomplete or inaccurate information by the borrower or their broker. This is then 'discovered' during the appraisal process. Which changes the outcome and the banks underwriting, and the appraiser is indirectly blamed or seen as responsible for delivering a lowered value.

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

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

1. Inadequate consideration of the quality of service, or geographic or market competency of the appraiser.
2. Federal regulatory agencies remain deeply under-resourced to deal with examination issues involving real estate appraisals. At one point in the 1990s, each federal regulatory agency had competent appraisers on staff helping to support examination teams. Today, there are no professionally designated appraisers supporting examination functions in the four major examination agencies. There is ample room for enhancement here, as examiners face a wide variety of collateral valuation challenges today.
3. Generally, most banks have opted not to take responsibility or ownership of residential appraisal functions, instead electing to outsource appraisal operations to third parties that offer a perceived layer of insulation from coercive pressure but apply new business pressures that put constraints on appraisal quality. Further, use of appraisal management companies can add to the time it takes for a bank to finalize appraisal review within a loan application.

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

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

Section 1492 of the Dodd-Frank Act explicitly requires creditors and their agents to pay "customary and reasonable" fees to appraisers to reflect what an appraiser typically would earn for a residential appraisal assignment absent the involvement of an appraisal management company. Under the Act, evidence for such fees may be established by objective third-party information, such as government agency fee schedules, academic studies and independent private sector surveys. There is sound reason for this provision. Specifically, it helps to assure that faulty appraisals will not give rise to the sort of financial crisis that this country faced a decade ago.

The rules promulgated by the Federal Reserve (Interim Final Rule) and the Consumer Financial Protection Bureau (Final Rule) contradict the plain language and intent of the Dodd-Frank Act. Two presumptions of compliance are provided by the Federal Reserve and accepted by the CFPB that are internally inconsistent. One presumption requires independent studies or fee schedules that align with retail appraisal fees direct from the appraiser, while the other accepts internally generated results that include what amounts to wholesale fees involving third parties.

Even as the CFPB has finalized the original Interim Final Rule unchanged, we continue to have concerns with the internal inconsistencies found in the two presumptions for compliance, and we urge fresh oversight on this issue and the related issue of consumer disclosure of appraisal and AMC fees.

Consumer Disclosure
The congressional requirement that customary and reasonable fees be paid to appraisers is undermined by consumer disclosure rules that allow the co-mingling of appraisal and appraisal management company fees on the Appraisal line of the Consumer Disclosure form issued by the CFPB. This co-mingling confuses consumers into believing they are paying appraisers more for services today, when, in fact, compensation levels may have significantly declined because appraisal management companies are taking a sizeable portion of the total cost paid by the consumer.

The Dodd-Frank Act authorized the CFPB to require the disclosure of AMC fees separately from fees paid to appraisers. In developing the final "TRID" rule, the CFPB conducted consumer testing of sample Closing Disclosure forms. This testing concluded that consumers were indifferent to the disclosure of AMC fees separately from appraisal fees, indicating that consumers were not confused by a disclosed appraisal management company fee. Despite this, in the final rule, the CFPB erred on the side of less disclosure, allowing – but not requiring - AMC fees to be reported separately from appraisal fees. As a result, most lenders continue to comingle AMC fees with appraisal fees. We continue to believe consumers are better off being fully informed about fees they are paying.

Question 3: How is technology changing the appraisal industry and are there concerns with some of the changes that are occurring as a result of evolving technology?

Technology has made, and continues to make, the appraisal process more efficient in some ways, and possibly more complicated in others. A bevy of data and software applications are widely available to appraisers to assist with virtually every facet of the appraisal process, from client communication to data acquisition and appraisal reporting. We do not track a metric on productivity or efficiency, but appraisers are more efficient today than ever before. Appraisers are also some of the first adopters of technology in the real estate sector.

Within the appraisal process itself, some factors may be replaced by technology. Auto-population of data from data systems like the multiple listing services has removed much of the need for manual entry of data, for example. Some factors may be enhanced by technology. Our organization has offered seminars on drones in real estate appraisal, and we have a new seminar on big data or "artificial intelligence" in real estate appraisal, as examples. Still, other factors simply cannot be replaced, or face severe limitations. The ability to analyze and observe functional obsolescence in a property is one such example. Positive features like view amenities, high quality construction features, green features, etc. are also observations by the human eye that cannot be replaced with technology. Remember, that appraisal is an applied study objectively based on careful analysis and judgement. Those factors cannot be easily replaced by machines.

Technology can also be misused. Automated valuation models can be programmed to produce predetermined outcomes. The lack of quality standards on AVM modeling is potentially a risk.

Appraisal Waivers

Today, Fannie Mae and Freddie Mac waive appraisals in certain circumstances based on automated valuation models and internal models and systems. These systems are fed, substantially in part, by data extracted from appraisals completed by appraisers across the country. These systems were established following the financial crisis largely to conduct a level of quality assurance on the appraisal before purchase the loan from a loan seller. Prior to the crisis, the GSEs did not see the appraisal report and delegated nearly the entire appraisal due diligence process – including review – to the loan seller. That was not a healthy arrangement.

While we support more quality assurance by the GSEs, we do not want to see competition between the enterprises result in a race to the bottom on risk management. The enterprises should not compete based on who can do less due diligence, for example. We have raised these concerns directly with the enterprises and the FHFA, and we have been told that plans to use such waivers are said to be generally limited in scope or based on factors such as risk and availability of data. However, we note that if fewer appraisals are done by appraisers, these systems will no longer be fed good data. In the longer run, any AVMs using such data will become less reliable.

Fannie Mae and Freddie Mac are in a position where they can provide some neutral information to appraisers that would be beneficial to the appraisal process. Simple things such as what type of records exist for square footage would be extremely helpful to an appraiser, who could verify which record is correct. We have also discussed this idea with the GSEs, and the general concept seems part of the ongoing review of the modernization effort.

Hybrid Appraisals

Fannie Mae and Freddie Mac have undertaken two related initiatives in appraisal – to "modernize" the appraisal process and develop new appraisal report forms. Both are multi-year efforts and relate to the data aggregation and appraisal waiver issues identified above. The report forms project is essentially an identification of the data package that the GSEs want to collect from the appraisal, along with how the appraisal report form might be made more dynamic or functional to the appraiser or the appraisal process. We have provided feedback to the GSEs on the appraisal report forms project, and we look forward to continuing to work towards improvements to the appraisal report forms.

The modernization project appears to center on the potential development of "gap" products for appraisals. There are essentially two appraisal order options for the GSEs today – the Uniform Residential Appraisal Report (Form 1004/70) or an appraisal waiver (none). In the past, various efforts to develop gap products were met with mixed results.

In discussing the issues with the GSEs, much of the current effort appears centered toward a goal of reducing turnaround times with appraisals. With this, we understand the GSEs have tested and evaluated various "hybrid" or "bifurcated" appraisal processes that may involve different work forces for completing the inspection of the subject property. Rather than the appraiser or someone associated with the appraiser (an associate or trainee for example) completing an inspection of the subject property, that service may be completed by labor forces outside of appraisal, such as insurance inspectors or real estate agents. Once that inspection is completed by a third party, it would be delivered to an appraiser for a desktop analysis. Such an assignment can be performed by an appraiser. We would point out, however, that given the intended use of the appraisal, such as for loan collateralization, a more in-depth scope of work, such as a traditional appraisal may be necessary.

Not knowing or understanding the use or volume of the proposed bifurcated product is one concern we hear from appraisers. Risk based application of such scenarios may have merit, but we also see a potential slippery slope for a degradation of appraisal risk management. Furthermore, if there is a proliferation in the use of a bifurcated process, then it begs two questions. First, as analysts will not be in the field on a regular basis, how will appraisers overall maintain their edge and knowledge of the market along with real estate products in general? Second, and this is particularly critical, how will trainees gain adequate knowledge and experience in their markets. Maintaining one's edge and knowledge of the market on a recurring basis is important in terms of accurate valuation.

While we understand that GSEs are attempting to shorten the loan decisioning process, using competent appraisal professionals is tantamount to maintaining independence of the process and overall risk mitigation. We must work together to attract qualified individuals to the profession. We fear, users of appraisal services will run a race to the bottom in terms of capability and knowledgeable appraisers. We hear repeatedly that well-trained and independent professionals continue to move away from performing appraisal work for the financial services industry. Competent professional appraisers cannot afford to operate with the same cost structure, including liabilities, with diminished earning potential.

Appraisers express concern about changing processes and procedures, in part, because of their experiences with mortgage lenders leading up to and during the financial crisis. Virtually every lawsuit brought by the Federal Housing Finance Agency against mortgage lenders following the financial crisis involve various forms of mismanagement of the appraisal process by loan officers, mortgage brokers and others. Even this week, a major settlement was reached between the Federal Housing Administration and one of the nation's largest mortgage lenders over appraisal management failures. If the financial crisis taught us anything it is the importance of risk mitigation, and we see signals we are losing sight of this less than a decade removed from the largest financial crisis in a generation.

There are also significant concerns about liability we have raised directly with the GSEs. As the appraisal process is separated or bifurcated, the appraiser is being asked to evaluate the work of unrelated third parties. We believe it is critically important to recognize the distinction between "believing" third-party information in reliable, versus "knowing" that such information is reliable. Today, using extraordinary assumptions by appraisers helps reduce liability to the appraiser and has long been established in appraisal and lending practice, including federally related transaction appraisals. We believe it should continue to be recognized in any bifurcated appraisal process.

Further, we understand the GSEs may be considering utilizing third party inspection vendors who may not have certain liability coverage, including Errors and Omissions insurance coverage, for their work. Frankly, the best way to address this issue is through <u>indemnification</u> to the appraiser for the portion of the assignment relating to the inspection. This would remove most liability concerns altogether and help promote acceptance of this proposed process.

Absent this, we believe inspectors envisioned under the program should be held to the same standard as appraisers in having to stand and defend their work through such measures as carrying Errors and Omissions (E&O) insurance coverage. Some might say that the Seller/Servicer Guides do not require appraisers to carry E&O insurance. However, this overlooks that E&O coverage has been a de facto loan seller requirement for several decades now. It is a well known fact in the industry that an appraiser cannot get work from any lender if the appraiser does not carry E&O insurance.

Using alternative workforces to complete inspections is another concern, when viable appraiser-related alternatives are readily available. Appraiser trainees are a good example of this. They need to be envisioned as one potential source for inspections, however, lender/loan seller policies continue to stand in the way of their use. While the GSEs have tried to clarify their policies relative to the allowance for trainee inspections, many loan sellers continue to prohibit this practice today. This could be addressed with an altered policy to restrict loan purchases from loan sellers who prohibit trainee inspections.

I say this, acknowledging there are opportunities for some appraisers within this proposed bifurcated process. Specifically, such a gap product may be a viable substitute to alternative valuation services commonly found in the marketplace in such areas as portfolio monitoring and asset management. From a risk mitigation and consumer protection perspective, it is critical that a bifurcated process be used sparingly, not as the typical standard. There may be other efficiencies beneficial to appraisers, and we look forward to trying to resolve these and other issues with the GSEs and FHFA.

TRID Constraints
As we discussed above, technology in appraisal is usually driven by one factor alone – to reduce turnaround times. Today, the mortgage industry is adopting technology at a rapid pace. We live in a world of instantaneous loan approvals, and the mortgage and real estate industries are under intense regulatory pressure to comply with federal bank and consumer laws, increasing pressure on the closing process. Tight constraints around the Loan Estimate and Close Disclosure forms relating to appraisal exacerbate these issues, and sometimes inhibit the appraisal process itself.

In particular, the new TRID rules place unreasonable constraints around appraisal service fees we believe should be modified by Congress. Under the final TRID rules, appraisals are no longer in a 10 percent tolerance bucket, and only if a valid changed circumstance occurs can the cost of an appraisal to the borrower exceed what was disclosed on the Loan Estimate. Appraisers are asked to bid on assignments without understanding the complexity of the assignment. The problem with this is that it is difficult to understand the complexity of the assignment from a desktop. It is much like asking an architect to develop an architectural plan for a house without seeing the land.

Every appraisal assignment is different. There are, of course, acceptable ranges of scope of work and associated fees, but we believe it is unreasonable to ask appraisers to bid on an assignment sight-unseen. We recommend Congress reevaluate this requirement relative to appraisal costs.

Question 4: How diverse is the appraisal industry and what is being done to promote diversity in the industry?

We publish a fact sheet on the appraisal profession that contains broad demographic information in the United States. I am including with this testimony.

The Appraisal Institute maintains an Education and Relief Foundation (AIERF). For more than 50 years, the Appraisal Institute Education and Relief Foundation (AIERF) fostered the advancement of the real estate appraisal profession and played a critical role in supporting valuation education. AIERF supported a vast range of initiatives, from world-renowned resources such as the Y.T. and Louise Lee Lum Library, to programs that will help secure the future of the valuation industry, including research grants and scholarships. The AIERF Minorities and Women AI Course Scholarship is designed to provide financial assistance to help Candidates for Designation in advanced designation states achieve their designation. The AIERF Minorities and Women Education Scholarship is awarded to minority and women undergraduate students pursing academic degrees in real estate appraisal or related fields.

The Appraisal Institute also maintains a Minority and Women Directory in the Appraisal Institute's Find an Appraiser function. The Minorities and Women Directory is a search tool for local, state, and federal agencies and financial institutions that would like to, or are required to, assign a portion of their work to qualifying minorities, women and persons with disabilities. Designated members and Candidates for Designation of the Appraisal Institute can add themselves to this directory for increased visibility.

The Appraisal Institute also continuously undertakes professional recruitment efforts, including a release last month that highlighted professional career opportunities, including our involvement with the "Careers Building Communities" initiative with leading national real estate organizations. The corresponding website to this initiative allows visitors to navigate through the scores of career paths across all sectors of real estate. The Appraisal Institute's section of the website outlines why students and others should consider a career as an appraiser. The website is a collaboration of 29 real estate industry organizations, representing more than 10 million jobs, that focuses on raising awareness and attracting diverse talent to the industry.

Beyond this, a representative from the Appraisal Institute recently participated in a workshop in Baltimore, Maryland hosted by Fannie Mae and the National Urban League promoting the appraisal profession to minority communities. Both residential and commercial appraisal practices were discussed and highlighted. We understand this event resulted in the Appraisal Institute representative hiring an attendee as an appraisal trainee with his firm.

Question 5: Why are we seeing an undervaluation of properties in minority communities and what can Congress do to ensure that appraisal methodologies are not resulting in unfair valuations?

This question is complex and weighty, and the issues stretch well beyond appraisal.

Let me start by saying that appraisers report what is occurring in the marketplace. Appraisers do not make the market but reflect buyer and seller behavior in real estate. Appraisers do not evaluate individuals or borrowers; rather, they analyze the property markets. Appraisers work under various definitions, including a definition of "market value." Simply stated, market value is market value in the eyes of professional appraiser. Essentially, market value means, if you place a sign in the yard, what should the property sell for?

Our ethics requirements, which are enforced as law at the state level, require appraisers to perform their work with impartiality, objectivity and independence and without bias. Appraisers also must not use or rely on unsupported conclusions relating to characteristics such as race, color, religion, national origin, gender, marital status, familial status, age, receipt of public assistance income, handicap, or an unsupported conclusion that homogeneity of such characteristics is necessary to maximize value.[1] These ethics requirements have a long and vast history, and they have grown stronger since our profession was established almost a century ago. This theme is and has been strongly emphasized in appraisal education and the body of knowledge of the Appraisal Institute

A vast amount of research has been done on fair housing and housing development. Many have commented on how our mortgage finance system was developed and maintained to support liquidity of suburban housing stock, and how it may have neglected urban and rural areas. These are discussions well beyond the realm of appraisal.

Access to credit and mortgage financing is a subset of, or related to, the fair housing issue, and there is a discussion to be had on how appraisal interacts with mortgage lending and underwriting today. Mortgage lending practice is governed by a set of rules established by the secondary market and government agencies. These guidelines are often interpreted by lender underwriters and reviewers as "rules" to be enforced relative to the appraisal process. As a result – whether we are discussing inactive or limited markets, urban or rural markets, or new markets, such as "green" or energy efficiency valuation – we often hear that appraisers feel hamstrung by these guidelines or de facto rules.

This has resulted in a situation where nobody "owns" the problem. Appraisers will say they cannot go outside of a neighborhood to evaluate comparable sales to avoid being second guessed by underwriters. Such practice flies in the face of what we teach: that sales comps should come from the market area, which may or may not be the same as the neighborhood. AMCs and reviewers will say that the guidelines require the appraiser to demonstrate market reaction, and this is read to mean, "no sale/comp = no value." Meaning, the appraiser is asked to find comparable sales that simply do not exist because of inactivity in that market. Further, the secondary market and agencies will say, the problem is beyond their mission or scope.

We see an opportunity to make lender/underwriter guidelines fewer rules oriented and more flexible about the appraisal review process. Lender/underwriter guidelines need to stay out of the "how to do an appraisal" arena and defer to the appraisal profession's body of knowledge on appraisal practice matters. While the sale comparison approach in appraisal is likely the most reliable approach used in an owner-occupied housing scenario, it is not the only approach that should be accepted by lenders and underwriters. In an absence of comparable sales, cost and income techniques can be helpful in supporting adjustments in the sales comparison approach. This should be affirmed throughout all of mortgage guidelines.

Our members also report positive experiences in dealing with credit enhancement programs such as those established in Detroit in recent years and recently announced in St. Louis. These "Greenlining" funds provide

[1] USPAP 2018-2019, page 7, The Appraisal Foundation

secondary forms of financing – essentially a second line of consumer credit – based on a range of factors, and placed on top of the first note, which relies on the market value of the subject property. This program may be very helpful in generating market activity, which can then be used by appraisers as subsequent or future comparable sales in the market. Many of these markets are challenged due to lacking sales activity.

The idea of a Greenlining Fund may be a way to help this process move forward.

Pending Legislation

There are two bills before today's hearing we have been asked to provide comments on. One bill, introduced by Rep. Brad Sherman (H.R. 2852), involves FHA appraisals, while the other – a discussion draft - relates to registry fees established by the Appraisal Subcommittee.

The Rep. Sherman bill would allow licensed appraisers to do FHA appraisals. We support this bill because it addresses long-standing concerns about the implementation of pre-existing FHA appraisal requirements, which are unique and differ from those of the GSEs and the conventional market. As background, the HERA Act of 2008 last amended the FHA requirements, and it required that state certified appraisers or those certified by a nationally recognized appraisal organization be eligible for the FHA Appraisal Roster. We supported the intent of the HERA Act because FHA was ramping up efforts to capture more market share in the mortgage market. At one point, FHA represented less than half of the lending market; now, it exceeds 25 percent by some estimates. Leading up to this, the requirements for FHA Appraisers had been continuously watered down by the agency, first, an exam requirement was eliminated, and then an education requirement was removed. The HERA Act attempted to raise the bar to help protect the FHA Insurance Fund by elevating the FHA appraiser requirements to state certification and those who have demonstrated verifiable education on FHA appraisal requirements.

The implementation of the HERA Act is what has been at issue over the decade. Some creative lawyering by the agency has avoided implementation of the verifiable education provision, accepting the requirements for state certification for the FHA appraisal requirements. The problem is that the state certification requirements do not cover the FHA appraisal requirements.

We believe if the FHA is going to maintain a separate set of requirements for FHA appraisals that appraisers should demonstrate understanding of those requirements. Taking a course in FHA appraisals is not an unreasonable burden and far exceeds self-attestation by the appraiser, which is essentially all that is required today by the FHA.

A similar bill has been introduced in the Senate by Senators John Thune and Jon Tester (S. 1722). It covers the same issue but does not apply the verifiable education requirement to all FHA appraisers. We support the spirit of this bill too and we understand discussions have taken place to resolve differences. We believe it would be more meaningful to apply these requirements to all FHA appraisers; those who have taken a previous seminar on the FHA appraisal requirements would satisfy the provision, and if some time were needed for implementation, we suggest one certification renewal cycle could be given to appraisers and the FHA.

The second bill (a discussion draft) relates to registry fees established by the Appraisal Subcommittee. The Dodd Frank Act authorized the Appraisal Subcommittee to establish a Registry for Appraisal Management Companies with a corresponding fee based on the number of appraisers on AMC approved appraiser lists. The Appraisal Subcommittee finalized the AMC Registry Fee rules in 2017 with a constrained interpretation of the Dodd Frank Act. The result is a fee potentially higher than what was envisioned during the drafting of the Dodd Frank Act. This bill would give the Appraisal Subcommittee authority to establish different formulas for the AMC Registry Fee. It would also allow the registry fees to be used for a broader array of programming, both concepts we can generally support. Last, the bill would allow the Appraisal Subcommittee to include appraisal trainees in the National Registry of Appraisers, charging up to $20 per year for such inclusion. The bill is written flexibly to give the Appraisal Subcommittee wide discretion in establishing a trainee registry fee. In theory, we could argue that the Appraisal Subcommittee could charge $1 for trainee inclusion. We continue to wonder, however, whether any fee should be charged for trainee inclusion in the National Registry, given the need and difficulty in attracting aspiring appraisers in the appraisal profession. We would be pleased to continue discussing this issue with the Committee and the Appraisal Subcommittee to find an appropriate solution.

Finally, this discussion draft also includes a provision that we recommended and strongly support – to mandate full disclosure of AMC and appraisal fees to consumers. This provision would rectify a shortcoming currently found in the new TRID rules and increase consumer awareness around the appraisal process (as explained above).

Additional Legislative Recommendations

As the Committee looks to build upon the two bills above, we urge continued review of these legislative suggestions that we believe would be beneficial to consumers, users of appraisal services, and professional appraisers:

1. Appraisal should be removed from the zero-tolerance bucket under TRID.

2. Establish parameters around rulemaking pursuant to the EGRPRA process. The latest EGRPRA review took several years to complete and resulted in recommendations since ignored. It is not unreasonable to expect rulemakings undertaken by the agencies to follow final recommendations from the EGRPRA review, and we would urge that some parameters be established around this to avoid a perpetual state of change in risk management.

3. Authorize the Appraisal Subcommittee to serve as a "negotiated rulemaking committee" to establish consistent and flexible lender guidelines relating to appraisals that would address issues such as inactive or limited markets where there is an absence of comparable sales. Such a consensus building committee could bring all agencies and stakeholders to the table to develop guidelines with greater consistency and understanding than today. Such guidelines could then be utilized by agencies and enterprises as their own, with deference given to any supplemental requirements that would correspond to their respective missions.

4. We continue to view appraisal regulatory reforms as essential to housing finance reform and helping to reduce red tape for practicing appraisers and users of appraisal services. We have discussed before this Subcommittee in recent years the idea of establishing a nationwide licensing system for appraisers, where appraisers could be afforded "one-stop shopping" for appraiser license application and renewals. Such a system would continue to work with state regulatory agencies, and would in fact, build and enhance their operations. Such a system could help share disciplinary action information from agencies or enterprises with state regulators. It could also help appraisers track continuing education renewal deadlines and help resolve concerns about portability of appraiser education.

   With the proper controls and oversight in place, the Appraisal Subcommittee could be tasked with managing such an assignment in conjunction with the Appraisal Foundation. This would represent a neutral project that would be beneficial to the entire appraisal profession and all its stakeholders. We urge this Committee to consider such an initiative under a more comprehensive appraisal reform measure that might include components of legislation referenced above.

Thank you for the opportunity to be with you today; I would be happy to answer questions that you may have.

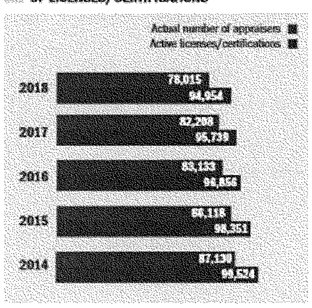
Appraisal Institute®

U.S. VALUATION PROFESSION FACT SHEET Q1 2019

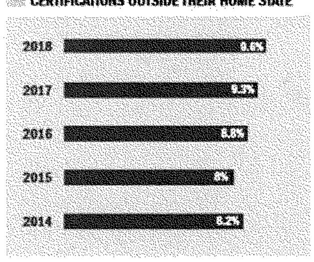
As of Dec. 31, 2018, the number of active real estate appraisers in the U.S. stood at 78,015, a decrease of 5% versus 2017.

The average rate of decrease for the past five years has been approximately 2.6% annually. Broader analysis suggests that declines may continue due to retirements, fewer new people entering the appraisal profession, economic factors, government regulation, and greater use of data analysis technologies.

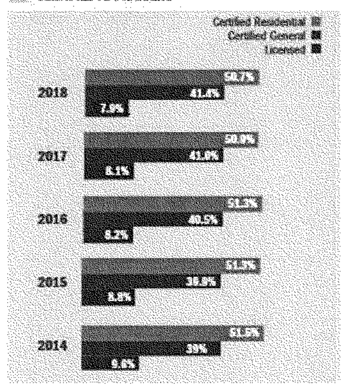
TOTAL U.S. APPRAISERS AND NUMBERS OF LICENSES/CERTIFICATIONS



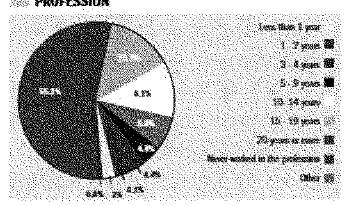
APPRAISERS WHO HELD 2 OR MORE LICENSES/ CERTIFICATIONS OUTSIDE THEIR HOME STATE



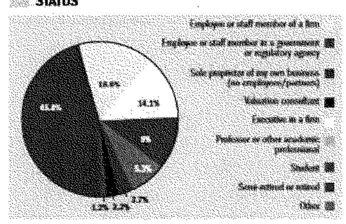
PROPORTIONS OF LICENSED AND CERTIFIED APPRAISERS



TIME IN VALUATION PROFESSION



EMPLOYMENT STATUS



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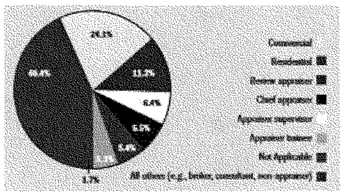
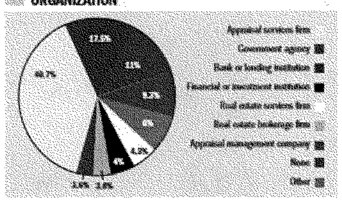
PRIMARY JOB FUNCTION



TYPE OF COMPANY OR ORGANIZATION



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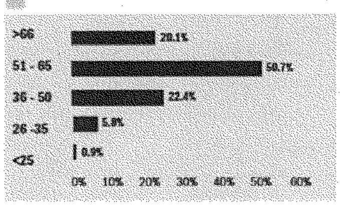
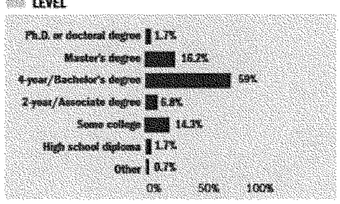


EDUCATION LEVEL



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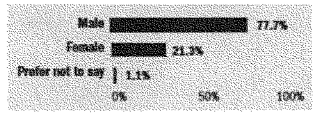

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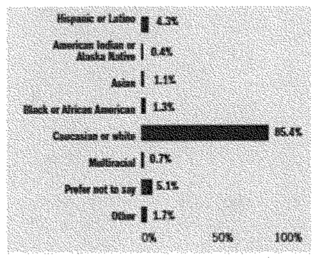
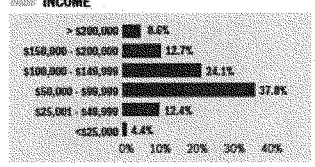


ANNUAL INCOME



U.S. appraiser population statistics were derived from the ASC National Registry as of Dec. 31, 2018. Additional demographic statistics were derived from Appraisal Institute studies conducted in 2016-2019 that were comprised of randomly selected AI and non-AI real estate valuation professionals. In Q1 2019, the Appraisal Institute invited 15,600 valuation professionals, resulting in 750 responses. This survey's margin of error is approximately +/- 3.56 percentage points at the 95 percent confidence level.

The Appraisal Institute is a global professional association of real estate appraisers, with nearly 18,000 professionals in almost 50 countries throughout the world. Its mission is to advance professionalism and ethics, global standards, methodologies, and practices through the professional development of property economics worldwide.