

THE BEST LAID SCHEMES



by Rachel Bailey and Andrew Kantor

QUICK QUIZ: WHAT new set of requirements caused these gentlemen to make the following comments?

Chris Call, an appraiser with Areas Appraisers in Springfield and chair of VAR's Appraisal Alliance: "The past two months have been the least pleasant in terms of how we deal with people."

Jamey Leonard of Appraisal Services of Virginia in Roanoke: "They've taken the mortgage broker out of the mix and basically inhibited free trade in this industry."

Pat Turner, owner of P.E. Turner & Co. and former member of the Virginia Real Estate Appraisal Board: "It is price fixing, in my opinion."

Answer: The HVCC — the Home Valuation Code of Conduct. Some would say it's the latest four-letter word to enter the lexicon.

Agents hate it.* Independent appraisers hate it.* Legislators are getting an earful about it. Realtors® are trying to deal with it — and complaining loudly and clearly. NAR wants a moratorium on it. And VAR's Public Policy Committee is looking at new regulations that might lessen the impact it's having.

How did a regulation — not even a law! — meant to make things better end up causing this much angst? (So much so that many of the things people told us when discussing the HVCC were unprintable.)

The answer is a combination of unintended consequences and a lot of misinformation.

** No, not every agent hates it, nor every independent appraiser. But, based on the feedback we've gotten, the vast majority are at least very unhappy about the HVCC.*

GOOD INTENTIONS

In 2007, New York Attorney General **Andrew Cuomo** sued eAppraiseIT (an appraisal management company owned by First American), accusing it of colluding with Washington Mutual to hand-pick appraisers for properties — appraisers that would give the bank the valuations it needed to make some deals work.

Cuomo said at a press conference, “By allowing Washington Mutual to hand-pick appraisers who inflated values, First American helped set the current mortgage crisis in motion.” (A bit over the top, perhaps, but that’s what he said.)

Instead of fighting in court, a settlement was reached. As part of that settlement, Fannie Mae and Freddie Mac agreed to adopt a set of rules spelling out how appraisals would need to be handled for any mortgage they were part of — i.e., just about all of them. And thus was born the HVCC. (Eleven months later, WaMu was taken over by the U.S. Office of Thrift Supervision and closed.)

The HVCC’s primary purpose: to keep lenders and appraisers honest by limiting the chance that the appraisal process will be influenced by someone who’s part of the *loan* process. According to the Federal Housing Finance Agency, “The HVCC is designed to promote professional appraisals free from inappropriate pressure from lenders, borrowers or brokers.”

Quoth the HVCC itself:

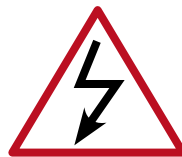
“No employee, director, officer, or agent of the lender, or any other third party acting as joint venture partner, independent contractor, appraisal company, appraisal management company, or partner on behalf of the lender, shall influence or attempt to influence the development, reporting, result, or review of an appraisal through coercion, extortion, collusion, compensation, inducement, intimidation, bribery, or in any other manner.”

Considering the headaches it’s caused, the HVCC is short — only four pages. Those pages build (or try to build) a wall between lender and the appraiser. More specifically, between the lender’s loan-production staff and the appraiser.

Yet the HVCC gives the responsibility of hiring the appraiser to the lender.

“The lender... shall be responsible for selecting, retaining, and providing for payment of all compensation to the appraiser,” it says. Further, the lender can’t use a report from an appraiser “selected, retained, or compensated in any manner by any other third party (including mortgage brokers and real estate agents).”

So the lender is supposed to hire the appraiser, but not have anything to do with the hiring?



The HVCC doesn’t apply to all appraisals, only to one- to four-unit single-family loans sold to Fannie Mae by mortgage originators.

Yes.

Enter HVCC’s “wall.”

The HVCC forbids any member of a lender’s *loan production staff* — and anyone who might profit from “the successful completion of the loan” — from having anything to do with choosing an appraiser.

So while the lender is responsible for choosing and paying the appraiser, it is supposed to clearly separate that process from its actual lending. Thus the loan production staff is forbidden from “having any substantive communications with an appraiser or appraisal management company relating to or having an impact on valuation, including ordering or managing an appraisal assignment.”

If that sounds like a questionable proposition, you’re not alone in thinking that. **Craig Butterfield** of Craig Butterfield & Associates, an appraisal company in North Carolina, equated it with hiring the fox to guard the henhouse.

ASKING FOR TROUBLE

The first questions, of course, are these: Did the appraisal rules need to be changed, and did they need to be changed that much? It’s hard to find someone who’ll say “Yes.” The consensus instead tends toward the word “overkill.”

“From my perspective, because a fix was made for the actions of a very few, the negative impact to many has been catastrophic,” Chris Call says.

But doesn’t the WaMu debacle show that the appraisal process clearly needs more oversight?

“Having been on [Virginia’s] Real Estate Appraisal board from 2001-2005, there’s plenty of oversight,” Call says. “The board is receiving cases all the time and reacting with suspensions, fines, required continuing education — there’s plenty of oversight.”

And **Mack Strickland**, president of Strickland Appraisal in Chester and incoming chair of NAR’s Appraisal Committee, says he thinks “it’s much to-do about nothing...what it has accomplished is that they’ve taken appraisers who have had long-time experience with mortgage brokers...out of the loop.”

And when it took the brokers out of the loop, the HVCC presented lenders with a conundrum: They were now responsible for hiring appraisers, but they had to

insulate themselves (or at least their loan production staff) from that process.

So they turned to a buffer: appraisal management companies. AMCs serve as brokers for individual appraisers. The bank hires the AMC, and the AMC has a list of approved appraisers. It typically takes the next name from its list (although such a rotation isn't required) and sends that appraiser out to the site. The bank is insulated from the process.

What could be wrong with that?

WHAT THE TRAFFIC WON'T BEAR

With so many lenders turning to AMCs, it gives those companies a lot of control over the process and the price. They decide not only what to charge the lender, but what they're willing to pay the appraisers.

Appraisers and appraisal companies who had developed solid, professional working relationships with brokers over the years found all that experience flushed down the tubes.

"It's had a very negative impact on our business," Call says. "The relationships we've developed for years have been wiped out — our whole business model has been wiped out."

Although there are at least two bills in Congress dealing with HVCC, the chance of either going anywhere is small.

They now have to build from scratch relationships with an entirely new set of clients: The AMCs. And, they say, the defining standard with those companies isn't so much professional competence as price. (We tried to talk to AMCs for this story; only one was willing to comment on the record.)

If an appraiser meets the basic standards and is willing to work for what the AMC is willing to pay, chances are he'll make the rotation. But a top-of-the-line appraiser with years of experience and the fees to match? Good luck.

Take P.E. Turner & Co. It's been around a long time — Pat Turner's Virginia appraisal license number is 4 — but, he says, that didn't matter. What *did* matter was his fee, and it was too high for at least one AMC.

"My firm is the oldest, most well established firm in Central VA," he says, "and I've been blacklisted by [one large AMC] because," he believes, "I will not reduce my fee below the 'competitive fees' they're willing to pay."

Call also says he's been on the short end of the competitive-fee stick. "Appraisers who work with AMCs have

seen their gross receipts reduced in most cases," he says.

But don't be so quick to blame AMCs says George Vann, chief appraiser for LSI, a national AMC. "The HVCC is definitely not cutting out the appraiser," he says. And, he points out, it was the mortgage brokers' fault the HVCC came about in the first place.

"[T]hey did the loans and ordered their own appraisals and abused the privilege they had," he says. "They'd go out and order two or three appraisals until they got the one they wanted, and then that's the one they sent to the lender. I'm not saying it was all the time — there's good and bad [mortgage] brokers — but it was a problem."

But Vann does understand how appraisers feel. "I was an appraiser and I didn't like AMCs when I was appraising," but don't lump them all together. "You've got good AMCs and you've got bad AMCs, just like you've got good appraisers and bad appraisers. That's how you have to look at it."

QUALITY CONTROL

So who *is* working for AMCs? What you'd expect — a mix of experienced and inexperienced appraisers. What has some in the business gnashing their teeth is that the low fees so many AMCs seem willing to pay — that encourages appraisers with less experience while discouraging those who have been on the job longest. And that, they say, means consumers are more likely to get an appraiser with fewer miles under the belt.

"You've got a lot of appraisers who will not work for [those fees]. They just can't," Strickland says. "And you have some that do. These are the ones that are usually new, just starting out, getting work any way they can."

"Some of the ones willing [to work for the lower fees] are new to the industry," Jamey Leonard says. "Experience plays a lot into what's going on with them."

It's basic capitalism. As AMCs have more influence in the market (thanks to lenders not taking any chances with the HVCC), they effectively lower the price the market will bear for an appraisal. With less money coming in for each job, competition heats up. Appraisers need to be willing to go a little farther for a job and accept the fees the AMCs are willing to pay — or hope to get assignments from risk-averse lenders.

The result, people like Pat Turner say, is lower fees — but at the cost of experience.

It's simply a matter of math, he says. When you take into account driving to a site, the overhead of an office, plus insurance and incidental costs, it can feel like an

appraiser is working for fast-food wages. And that, he says, pushes out appraisers with the most experience.

Tony Whaley is eastern United States appraiser manager at Quantrix, an AMC that's a joint venture between First American and Chase. (And yes, banks own AMCs, which makes the whole 'separation between Church and state' even more complex.) Whaley agrees that the price an appraiser charges is a factor, but not at the cost of experience.

Yes, he has guidelines for how much he can pay, but, he says, appraisers who charge more "are not blacklisted, they just might not get as much work." After all, "You'll go to the store where you can get it cheapest. It might be the same product, you know."

In other words, Quantrix does look for quality. But if there are two appraisers for an area, both competent, and

one is lower fee than the other, he'll pick the lower fee, because, he says, fee doesn't relate to quality.

You won't get Turner to buy that logic, though. But worse than the issue of the fees AMCs pay is the idea that as the price the traffic will bear goes down, appraisers are more willing to take assignments out of the areas they know — and that's the other issue with the HVCC.

DON'T KNOW MUCH ABOUT GEOGRAPHY

The Realtor® Code of Ethics says that Realtors® should not accept a job in an area they aren't familiar with. That's why many will opt for making a referral. The same is true for appraisers. Even Fannie Mae makes it clear:

"If an appraiser is not knowledgeable about a particular location, is not experienced in appraising a particular type of property, or is not familiar with (or does not have



MISINFORMATION

There seems to be plenty of incorrect information about the requirements of the HVCC floating around — so much so that in June both the Appraisal Institute and NAR released 'HVCC myths and facts' flyers (Realtor.org/hvcc), and Fannie and Freddie published their own HVCC clarification.

THE HIGHLIGHTS:

MYTH: Appraisers don't need to come from or be familiar with an area to do appraisals there.

REALITY: Geographic competency is a requirement of the HVCC.

According to Fannie Mae, "[W]hen an appraiser signs Fannie Mae's residential appraisal report form, the appraiser is also certifying the following: "I have knowledge and experience in appraising this type of property in this market area." And "I am aware of, and have access to, the necessary and appropriate public and private data sources, such as multiple listing services, tax assessment records, public land records, and other such data sources for the area in which the property is located."

And no, that latter part doesn't mean, "I beg the listing agent for comps."

MYTH: HVCC prohibits Realtors® and lenders from talking to appraisers.

REALITY: Realtors® and lenders can talk to appraisers, including making requests to consider additional data or to correct errors.

"That's an ignorant appraiser who says 'I can't talk to Realtors®,'" Pat Turner says. "They can talk to us and we can talk to them. How else can I get in the house if I don't talk to the listing agent? How will I do an accurate market analysis if I don't at least interview the agent and get

their thought process on marketing the house at that price?"

Remember, the HVCC prohibits anyone from "influencing or attempting to influence the development, reporting, result, or review of an appraisal." It doesn't say they can't talk to an appraiser.

"I'm hired to do an objective opinion of value," Turner says. "But that comes with doing full research."

MYTH: A lender is required to use an appraisal management company to get an appraisal.

REALITY: Lenders may directly retain the services of an independent appraiser, as long as its loan-production staff is not part of the selection process.

Mack Strickland: "HVCC doesn't require lenders to use AMCs. What it boils down to is there needs to be some insulation between the loan officer and the AMC. So instead of the loan originator and the loan officer ordering the appraisal, they have someone in their office who calls to order the appraisal."

MYTH: Lenders are required to choose appraisers from a rotating roster approved by Fannie Mae or Freddie Mac.

REALITY: Lenders may choose to use a rotating roster of appraisers but are not required to do so by Fannie Mae or Freddie Mac.

MYTH: Appraisals are not transferable between lenders.

REALITY: Lenders can choose to transfer an appraisal; nothing in the HVCC prevents that. Lenders receiving such an appraisal are responsible for ensuring that the original appraisal met the HVCC's requirements.

access to) the appropriate data sources, a lender should not give the appraiser assignments in that market area or for that particular type of property.” That’s straight out of the *Fannie Mae Single Family Selling Guide*.

The logic is clear: It’s hard to estimate the value of a home in a neighborhood if you don’t know the neighborhood.

Before the arrival of the HVCC, mortgage brokers would turn to the appraisers they knew — appraisers who were familiar with the area a home was in. With AMCs running the show, however, the job can go to whomever is next on the list, no matter where that person is from.

Which brings up the catchphrase so many independent appraisers are using: geographic competence.

“I’ve spoken now to five different real estate offices here in Richmond and they’re all upset just because appraisers are coming in here from Virginia Beach and from Roanoke to do appraisals,” Turner says. “They don’t know the marketplace, they’re only picking up foreclosed sales, they’re not members of our MLS — they’re not geographically competent.”

Mack Strickland: “You have appraisers coming in to a market that they’re not familiar with, and they’re asking Realtors® to do a lot of the work, and even though they have a license that allows you to work anywhere in the state, you have to be competent.”

Anecdotes abound, mostly of the ‘way-out-of-line

valuation’ variety because of appraisers trying to work outside their areas, but also of appraisals taking much longer than before (attributed, rightly or wrongly, to inexperience). Call, for example, says that out-of-market appraisals often take longer because the appraiser needs to fix errors that a local appraiser wouldn’t make, and find information that a local appraiser would already have.

Elizabeth Greenfield, government affairs director for the Richmond Association of Realtors® says she’s “getting a lot of calls [about] the geographic issue.” And Suzy Stone, GAD for the Fredericksburg Area Association, echoed that: “It’s huge in Fredericksburg.”

The issue of geographic competence is so big that Fannie Mae and Freddie Mac issued a clarification of the HVCC on July 22, specifically discussing the issue of geography. The HVCC guidelines, it said, “require appraisers to have knowledge of the local market. The use of unqualified in-state or out-of-state appraisers, unfamiliar with local conditions, should be reported to state appraiser licensing agencies.”

And Quantrix’s Tony Whaley cautions that seemingly out-of-area appraisers may actually be local. “They might work for a company that’s out in Virginia Beach but they live in Richmond,” he explains. “I know an appraisal company that has employees living all over the state, but when one sends a bill out it’s going to say ‘Richmond’ on it.”

But while that might alleviate some concerns, it adds yet another layer of complexity to the HVCC mess. “It has become increasingly frustrating for Realtors®,” said Susan Gaston, government affairs director for the Williamsburg and Virginia Peninsula Realtors® associations. “It’s creating a situation where there’s such a feeling of distrust.”

And Call says he knows someone who calls it the “Home Valuation Crisis of Confidence.”

“We already had a code of conduct,” Call says. “We didn’t need another one.”

QUIS CUSTODIET IPSOS CUSTODES*?

Call, Strickland, and Turner all point out that appraisers *are* regulated, thank you very much. They must abide by the appraiser code of conduct — the Uniform Standards of Professional Appraisal Practice (USPAP).

“Realtors®,” says Pat Turner “have the Code of Ethics. They’ve got to be competent to handle a transaction. We have, under the USPAP, a set of conditions — the appraiser has to be competent too.” And competent, he said, includes knowing the location and even the submarket. Appraisers who violate it can find themselves facing



HVCC'S DEEP IMPACT

NAR Research asked its Realtor® and appraiser members how the HVCC has affected them. Some of the results:

- **76%** of real estate practitioners say the time to obtain a completed appraisal increased after May 1, the effective date of the HVCC.
- **69%** of those said those appraisal times increased by more than eight days.
- **37%** of respondents reported lost sales — 17 percent reporting one lost sale; 20 percent reporting more than one.
- **70%** of Realtors® reported an increased use of out-of-area appraisers.
- **39%** of NAR’s appraiser members reported more than half their assignments come from AMCs. Before May 1, only 14% said so.
- Half of appraisers asked reported receiving lower fees.
- **55%** of Realtors® reported a perceived reduction in appraisal quality; 85% of appraisers reported the same.

the Real Estate Appraiser Board. And USPAP's competency rule makes it clear:

"[A]n appraiser preparing an appraisal in an unfamiliar location must spend sufficient time to understand the nuances of the local market and the supply and demand factors relating to the specific property type and the location involved. Such understanding will not be imparted solely from a consideration of specific data such as demographics, costs, sales, and rentals."

Appraisers without that knowledge, USPAP says, should either *become* competent, work with a qualified local appraiser on the assignment, or decline it outright.

"We just had somebody disciplined by the REAB for going last month from Richmond down to Suffolk," Turner says. "Not only that, she then went to Eastern Shore to do an appraisal – from Richmond!"

But someone actually has to realize that an appraiser lacks that geographic competence in order for USPAP to be enforced. You would think that job would fall to the AMCs giving out the assignments, but, while appraisers are regulated, AMCs are not.

"Often, I am asked [by AMCs] to perform an appraisal assignment outside the areas I am most familiar with," posted one residential appraiser to the Appraisal Foundation's Web site, and "the assignments come with a requirement that a completed report be submitted within 48 hours or less."

Which is one reason there's a call for AMCs to be regulated by, say, the Real Estate Appraiser Board or even the Real Estate Board.

"Even the termite guy is regulated!" says Strickland. So AMCs should at least be required to meet the standards of the appraisers it hires, he says. The law should "require AMCs to hire local appraisers with geographic competence." The free-for-all that exists now has to go. "AMCs can be started by anyone," he points out, "including convicted felons."

It's not just the geographic competence issue that begs for regulation, either. From Turner's perspective, the best way to deal with all the issues is by regulating the AMCs. Because without someone watching them, he says, the situation will remain a messy one.

* "Who watches the watchmen?" What, you didn't take Latin?

THE PRICE ISN'T RIGHT

Stories abound.

The inland appraiser assigned to a waterfront property — he didn't know which features brought value to a waterfront home.



8 QUESTIONS YOU NEED TO ASK

Although AMCs aren't regulated, individual appraisers are — and they can be held to the regulation of the USPAP. Pat Turner suggests that Realtors® ask potential appraisers these questions:

1. How long have you been a real estate appraiser?
2. Are you licensed, are you certified, or are you a trainee appraiser?
3. What license do you hold?
4. Where are you from?
5. When was the last time you appraised a property in this neighborhood?
6. Do you know any of the local long-term Realtors® in this area?
7. After you inspect the property, how long will it take you to deliver the appraisal report to the lender? (It should be turned around within 48 to 72 hours unless it's an unusual piece of property.)
8. Are you a member of this MLS?

"The appraiser's answers are going to help that Realtor® gauge the competence of the appraiser in order to complete that assignment in a timely manner," Turner says. "If the lender is not going to insist on geographic competency, the Realtor® and borrower should."

Or the appraiser who asks for a copy of the sales contract ... and who produces an appraisal that matches it to the dollar.

"I just had an appraiser call me today and ask for a copy of the sales contract," says **Marty Martin**, a Realtor® with Wainwright & Co. in Roanoke. "I always want to ask, 'Why the heck do you need that?' It's amazing how many appraisals come in for the exact dollar of sales contracts. What are we using them for anyway?"

And, over and over, the same tale: Deals lost when buyers can't get a loan because the appraisal comes in too low for the bank.

Peggy James, who works with her partner, Eric Blackwelder, at Exit 1st Choice Realty in Woodbridge, is one Realtor® who's been hit hard by low appraisals. And, she says, it started suddenly, in May, just as the HVCC took effect.

"We had one appraisal come in \$70,000 low," she says. "The seller couldn't sell. The buyer couldn't buy. The deal fell through. The appraiser was from Maryland."

But is it possible, in this market, that the home *was*



overpriced? James doesn't think so.

"As a good listing agent you run the comps and formulate a solid value. Then a buyer's agent does the same," she points out. "How can all of the real estate professionals in the trenches of the real estate market be that far off base? And only in May and June of 2009?"

Yes, there's a lot of complaining, she says, but it's like air travel: Disasters get all the attention, but they're very much the minority.

It hurt. "We had five contracts blow up in one week," James says. "Never have we ever had anything like that. I almost left the business."

Stacy Magid of Coldwell Banker Elite in Prince William says that "not only are we having problems with appraisals being significantly lower than the comps in the area, but appraisers are putting a tremendous amount of ridiculous conditions on properties." And when appraisers start talking about painting or carpeting or cleaning, they're going above and beyond the call of duty, but not in a good way.

"We had one do a complete electrical critique," Magid says, "I don't believe the appraiser was a licensed electrician." And the worst part: "Many of these conditions are ridiculous and end up killing the deals."

But not every Realtor® is willing to put the blame on the HVCC or on appraisers.

"Let's not blow the new HVCC rules out of perspective," cautions Cindy Jones of RE/MAX Allegiance in Woodbridge. "Appraisal concerns were around before the new regulations and they will be around when this set of rules is replaced by another."

Yes, there's a lot of complaining, she says, but it's like air travel: Disasters get all the attention, but they're very much the minority.

"I just think that if you took all the sales that are happening and said, 'What are the percentage of the sales that have an appraisal problem?' we'd find the number wouldn't be that bad," she says.

And the deals nuked by a low appraisal? "How many of these are caused by the agents themselves?" Jones asks. How many agents are accepting offers that they know are too high, from buyers agents who want to get the offer accepted now, then deal with the price later?

"I had a listing in Lorton," she says. "I priced it at \$425,000, and I got an offer for \$465,000. I knew it wouldn't appraise nearly that high. We accepted an offer that was lower but that would appraise [at that value]."

And let's not forget that not too long ago the issue was appraisals being too *high*, Jones points out.

A few years ago, "one day a home was selling for \$400,000 and two weeks later the same house sells for \$425,000 with no questions about the value? Weren't appraisals part of the problem then as well?"

It's a matter of the seller's agent being careful about accepting realistic offers. "I've closed 16 transactions this year," she says, "and not a single appraisal problem."

Meanwhile, Peggy James hopes her luck begins to turn and there will be some change to the HVCC. "Hopefully the pendulum has swung too far to the left and it will come back again."

WHAT NOW?

Because of all the trouble the HVCC is causing, legislators and regulators are getting an earful, and changes are happening, if slowly.

NAR president Charles McMillan met in July with the New York Attorney General's office and the head of the Federal Housing Finance Agency to share NAR's concerns. That led to Fannie and Freddie's July clarification. NAR is also pushing Congress and the FHFA "to immediately implement an 18-month moratorium on the new HVCC rules to further address unintended consequences of this new rule."

In Virginia, VAR is looking at introducing legislation that would regulate AMCs, or at least put a certain burden of responsibility on them when it comes to assigning appraisers.

Call thinks even a basic change such as regulating AMCs (as appraisers themselves are regulated) would make a huge difference. And Strickland also thinks there are some simple solutions that could go a long way. For example, spot checks, where appraisers are told "give me three sample appraisals out of your file and let me approve them."

"I don't want to get them out of the business," he says. "I want to get them to conform to standards." ●