S. HRG. 108–869

THE REAL ESTATE APPRAISAL INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON HOUSING AND TRANSPORTATION

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

ON

CERTAIN PRIVATE ENTITIES AS OUTLINED IN TITLE XI OF THE FINANCIAL INSTITUTIONS REFORM, RECOVERY, AND ENFORCEMENT ACT OF 1989, THAT ESTABLISH UNIFORM RULES FOR REAL ESTATE APPRAISALS AND SET MINIMUM CRITERIA FOR CERTIFYING APPRAISERS

MARCH 24, 2004

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THE REAL ESTATE APPRAISAL INDUSTRY

WEDNESDAY, MARCH 24, 2004

U.S. SENATE,
SUBCOMMITTEE ON HOUSING AND TRANSPORTATION,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Subcommittee met at 2:33 p.m., in room SD–538, Dirksen Senate Office Building, Senator Wayne Allard (Chairman of the Subcommittee) presiding.

OPENING STATEMENT OF SENATOR WAYNE ALLARD

Senator ALLARD. The hearing will come to order.

I would like to welcome the panel, and as you can tell, we have some interest here on the Subcommittee about your subject matter today. We are looking forward to this afternoon and hearing from the panel. I would like to thank everyone for attending today's oversight hearing on the real estate appraisal industry.

Similar to the Global Crossing and Enron scandals of recent years, the 1980's brought the savings and loan scandal squarely before Congress. While the causes were numerous, the role of bad real estate appraisals could not be dismissed. Accordingly, when Congress drafted the Financial Institutions Reform, Recovery, and Enforcement Act, FIRREA, it included Title XI to create a new structure for the real estate appraisal industry.

It is certainly appropriate for Congress to become involved in the appraisal industry because of the clear Federal interest: Taxpayer dollars are at stake. In fact, the purpose of the law is to protect Federally insured financial institutions, not consumers. While a healthy industry can be of assistance to both, we must be ever mindful of protecting taxpayer dollars.

The new law looked at both sides of the industry for addressing both real estate appraisals and real estate appraisers. To do so, it utilized a complex relationship between Federal, State, and private entities. This relationship seems to have worked well in that it has stemmed the worst problems of the 1980's. However, that does not mean the law cannot be improved.

We are here today to get an update from the key players regarding the functioning of Title XI as well as their general views on the state of the industry.

First, we will hear from Dave Wood of the General Accounting Office. GAO completed a report on the real estate appraisal industry last year. He will be discussing their findings.

Next, we will hear from Steve Fritts, who will be testifying on behalf of the Appraisal Subcommittee of Federal Financial Institu-

tions Examination Council. The Subcommittee is responsible for monitoring Title XI compliance by all Federal, State, and private entities.

We will hear from Charles Clark, who is the Georgia Real Estate Commissioner and is here on behalf of the Georgia Real Estate Appraisers Board.

We will then hear from Dave Bunton of the Appraisal Foundation. The Appraisal Foundation is the private nonprofit entity charged with establishing uniform minimum criteria for appraiser certification and uniform standards for appraisal practice.

The next witness will be Alan Eugene Hummel, testifying on behalf of the Appraisal Institute. And finally, we will receive testimony from Eugene Kaczkowski on behalf of the American Society of Appraisers.

Before we begin, I would like to take a few moments to acknowledge my colleague from Georgia, Senator Miller. Senator Miller has been very interested in the issue of real estate appraisals for some time and has been quite active. In fact, I should point out that the GAO report I mentioned earlier was done at his request, along with that of Senator Sarbanes. I appreciate my colleague's dedication to a vigorous, healthy real estate appraisal industry, and I commend him for his work. I am pleased to have him here today, and I would defer to him for opening comments if he would like to make a more formal introduction of Mr. Clark, but first I would like to recognize Senator Reed and other Members. We all work under the 5-minute rule here, which is standard in the Banking Committee.

STATEMENT OF SENATOR JACK REED

Senator REED. Thank you very much, Mr. Chairman. Let me commend you for holding the hearing, and also commend Senator Miller for his very aggressive and tenacious efforts to have this whole area looked at and reviewed.

Title XI of FIRREA, as the Chairman points out, was created to oversee the real estate appraisal industry after the savings and loan collapse of the 1980's. In the last 15 years, it has been in operation. It is appropriate now to examine whether it is still working, whether improvements should or could be made to the regulatory structure set up for the real estate industry.

I look forward to the witnesses' testimony, and again, let me commend both the Chairman and Senator Miller for addressing this very important issue, and I yield my time.

Senator ALLARD. Senator Miller.

STATEMENT OF SENATOR ZELL MILLER

Senator MILLER. Thank you, Mr. Chairman. I would like to thank you, and I would also like to thank Chairman Shelby for holding this hearing today on the Real Estate Appraisal Reform Amendments.

As has been said, Title XI was adopted in response to faulty and fraudulent appraisals that contributed to the losses that the Federal Government suffered during the savings and loan crisis of the 1980's. Not long after I came to Washington in 2000 or early 2001, Mr. Steve Patton, with Lee and Grant in Atlanta, first brought the real estate appraisal issues to my attention. Mr. Patton was con-

cerned that the Appraiser Qualification Board, set up under Title XI, was setting fees too high for training real estate appraisers. Mr. Patton contacted the Georgia Real Estate Appraisers Board and they too were concerned.

States have the discretion to regulate the training, licensure, and discipline of professions that have an impact upon health and safety, such as nurses and physicians, but when it comes to licensing appraisers, Title XI imposed many more demands upon the States. This is one of the issues we asked the GAO to look into during its study, and I look forward to hearing what the GAO found.

Also Mr. Charles Clark, as you mentioned, Mr. Chairman, the Georgia Real Estate Commissioner, will discuss Mr. Patton's fee issue as well as other concerns of the Georgia industry.

Since Title XI was enacted, no one has looked at the State and Federal real estate appraisal systems and the effectiveness of the current structure. That is why Senator Sarbanes and I requested the GAO study and why we asked the Committee to evaluate whether a Federal protection is still necessary for real estate appraisers, whether the regulatory structure has become perhaps too complex and too burdensome. I believe the time has come to examine and debate the issues affecting the real estate appraisal industry. I am pleased that the Subcommittee has taken the time to hold this very important hearing today.

Finally, Mr. Chairman, I would like to welcome my fellow Georgian, Mr. Charles Clark, the Georgia Real Estate Commissioner, who will be testifying on this panel, and I thank all of you for being here who are going to testify.

Thank you, Mr. Chairman.

Senator ALLARD. I would like to recognize Senator Sarbanes, who is the Ranking Member on the Full Committee.

Senator Sarbanes.

STATEMENT OF SENATOR PAUL S. SARBANES

Senator SARBANES. Thank you very much, Mr. Chairman. First of all, I want to thank you and Senator Reed for holding this very important hearing, and also I want to thank Senator Miller for his strong interest in this issue. I joined with him in asking the GAO to do this study, and you will be hearing about that shortly.

I also want to express my appreciation to the members of the panel.

Unfortunately, I am not going to be able to stay because, as we all well know, I have conflicting engagements, but I did want to come if just briefly and make a statement because of the importance I attach to this issue of home appraisals.

In Baltimore City, which I am pleased to represent, and in fact where I live, we have been plagued by the problem of property flipping joined with predatory lending. This extremely noxious combination has resulted in neighborhoods that have been decimated by high levels of foreclosures and disinvestment, leaving the families who have been victimized by this scandal, families often headed by low-income, single, working mothers, without a place to live and with a credit profile that has been destroyed.

Regrettably, Baltimore has suffered from this problem at a scale greater than most other cities in large part because of the role of

some unscrupulous appraisers. Testimony given by the Assistant U.S. Attorney Joe Evans to the Baltimore Predatory Lending Task Force has been clear on this point. Mr. Evans said that bad appraisers are the enablers of this destructive and criminal process.

We are in the course of cleaning it up, thanks to the Predatory Lending Task Force and the very active work of the U.S. Attorney's Office.

This, in short, is how it works. An investor buys a foreclosed property for very little money, perhaps $20,000 or $25,000. He then makes very superficial repairs, if he makes any repairs at all; finds an unsuspecting homebuyer, often a person who cannot really afford or is not really prepared for homeownership. At the center of the scam is the unscrupulous appraiser, who is in on the fraud and appraises the property for $65,000, or $70,000. With that appraisal in hand, the investor helps the buyer qualify for a loan.

As soon as a problem pops up, a boiler breaks, a roof leaks, or the like, the homeowner finds herself in deep trouble and often defaults on the loan. The house is then sold at foreclosure sale for far less than the sales price, obviously, and the whole process starts again, resulting in further community disinvestment.

According to the U.S. Attorney's Office, once these property flippers identify an appraiser who is willing to participate in this outrageous behavior, that appraiser is then used in property after property by one bad investor after another. Now, these people are being prosecuted as they should be.

Further, I have spoken to a number of very reputable appraisers in Maryland who abhor and condemn this process, and who are working hard to eliminate these bad actors from their midst, but they need help.

Mr. Chairman, I commend you and Senator Reed for undertaking this hearing. We need to get a handle on this problem. I appreciate the work that the GAO has done to look at this issue. It is clear the current system is not fully adequate to the task, and I look forward to reviewing the testimony and the record of this hearing to see what steps may be appropriate for us to take at the Federal level, and what additional steps State and local authorities may take, and indeed, what steps the industry itself can take to, in effect, carve this pernicious behavior out of its midst. It is strongly condemned by all the reputable people in the appraisal industry as you would expect it to be, and I welcome that condemnation, but we have to figure out how we can get at these really bad apples, so they not only do not exploit people and tarnish them and victimize them, but also do not tarnish the workings of the many, many very able and dedicated people who are in the appraisal field.

Thank you very much, Mr. Chairman.

Senator ALLARD. I would like to call on the panel members, and as I mentioned in my opening comments, Mr. Wood, we will start with you, Director of Financial Markets and Community Investments with the U.S. General Accounting Office.

STATEMENT OF DAVID G. WOOD, DIRECTOR
FINANCIAL MARKETS AND COMMUNITY INVESTMENT
U.S. GENERAL ACCOUNTING OFFICE

Mr. WOOD. Thank you, Mr. Chairman. I apologize for my voice. I am getting over a bad cold.

Senator ALLARD. We will give you some relief on that voice. We will ask you to limit your testimony to 5 minutes, and then the rest of your statement, we will just submit that for the record.

Mr. WOOD. That will not be a problem.

My statement is based on our May 2003 report, which addressed three broad objectives: first, to describe specific responsibilities of each entity involved in the oversight structure established by Title XI; second, to determine what factors, if any, these entities identify as potential impediments to carrying out those responsibilities; and third, to identify concerns of the entities or industry participants about the effectiveness of the existing regulatory structure.

Regarding the first objective, Title XI specifies roles for private, State, and Federal entities. Instead of tasking a Federal agency to establish standards for appraisals or competency requirements for appraisers, Title XI recognized the work of two private organizations. These are the Appraisal Standards Board and the Appraiser Qualifications Board, which operate as part of the nonprofit Appraisal Foundation.

The Standards Board publishes uniform standards for the conduct and writing of appraisals. Title XI provides for all appraisals used in Federally related transactions to be prepared in accordance with these uniform standards.

The Qualifications Board establishes education, experience, and examination requirements for several categories of appraisers. Title XI does not require that all appraisers involved in Federally related transactions meet the Qualifications Board's criteria. Rather, it requires, with some exceptions, that such appraisers be either certified or licensed. The Qualifications Board's minimum criteria are used to certify appraisers.

Under the Title, States have the important responsibility of licensing and certifying appraisers. The States establish their own licensing criteria. The States are also responsible for monitoring and supervising compliance with appraisal standards.

At the Federal level, the five financial institution regulatory agencies are responsible for ensuring that the banks, thrifts, and credit unions they supervise comply with Title XI requirements. Among other things, these regulators specify which Federally related transactions require the services of certified appraisers, licensed appraisers, or neither.

And finally, another Federal agency, the Appraisal Subcommittee, is responsible for monitoring the implementation of Title XI by all parties, private, State, and Federal. Among other things, the Subcommittee periodically reviews each State's certification and licensing program, is authorized to make grants to the Appraisal Foundation to help defray the cost of the two boards, and is required to monitor the practices, procedures, and activities of the Appraisal Foundation.

Regarding our second objective, officials of these entities described several factors that could constrain their ability to carry

out their Title XI responsibilities. For example, officials of the Standards Board and the Qualifications Board stated that insufficient Federal grants could impede their future ability to ensure that standards and qualifications evolve with changing marketplace conditions.

State appraiser agencies, which we surveyed with a questionnaire, reported resource limitations as their primary impediment. As an example, 26 States reported having an insufficient number of investigators.

Finally, the Appraisal Subcommittee reported that additional enforcement sanctions could help its efforts to oversee State compliance. We did not assess the extent to which these factors would impede the goals of Title XI, but did add contextual information where possible.

In response to our third objective, we identified a number of concerns, including: The lack of a national qualifications standard for licensed real estate appraisers and other differences among State licensing programs; the cost and lack of uniform approval processes for appraiser education courses; the potential reluctance of lending institutions to make referrals of questionable appraisals they identify to the States for action; and a lack of consistent and effective enforcement actions by the States on cases that are referred.

Many of these concerns reflect the almost inevitable tension that exists when a statute attempts to balance both Federal and State interests. We noted no clear consensus on the need for or impact of possible changes to the overall regulatory structure. However, we did identify actions that we believe could enhance the effectiveness of the existing structure.

Accordingly, we recommended that the Appraisal Subcommittee, among other things, develop and apply consistent criteria for determining and reporting the States' compliance with Title XI, explore options, including drawing on its surplus, if necessary, for future grants to the Appraisal Foundation, and to coordinate with Fannie Mae, Freddie Mac, and HUD to improve the process of referring problem appraisals to the States for enforcement. The Subcommittee has reported that it is acting on these recommendations.

Mr. Chairman, that concludes my prepared statement. I will be happy to take questions.

Senator ALLARD. Thank you. You stayed pretty well within our 5-minute limit. The timer that we have up here, when the caution light turns on—you have one there on your table—it gives you about a minute to wrap up. It turns at four, and then at five.

Mr. Fritts, you are next. Mr. Fritts is Associate Director of Risk Management/Examination Support Division of Supervision and Consumer Protection, Federal Deposit Insurance Corporation, and you are testifying as Chairman of the Appraisal Subcommittee of the Federal Financial Institutions Examination Council.

Mr. Fritts.

STATEMENT OF STEVEN D. FRITTS
CHAIRMAN, APPRAISAL SUBCOMMITTEE,
FEDERAL FINANCIAL INSTITUTIONS EXAMINATION COUNCIL
ASSOCIATE DIRECTOR,
RISK MANAGEMENT/EXAMINATION SUPPORT,
DIVISION OF SUPERVISION AND CONSUMER PROTECTION,
FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. FRITTS. Good afternoon, Chairman Allard and Members of the Subcommittee. Thank you for the opportunity to discuss the current state of the appraisal industry and its Federal and State oversight. On behalf of the Appraisal Subcommittee, which I currently chair, we commend your Subcommittee's initiative to assess the industry.

The Appraisal Subcommittee oversees the real estate process as it relates to Federally related transactions. Its membership includes the representatives from each of the five members of the Federal Financial Institutions Examination Council, which includes the FDIC, the Federal Reserve, the Office of the Controller of the Currency, the Officer of Thrift Supervision, and the National Credit Union Administration. Also a representative of Housing and Urban Development serves on the Subcommittee.

Following the financial crisis of the 1980's, Congress passed the Financial Institutions Reform, Recovery and Enforcement Act of 1989, informally known as FIRREA. Title XI of FIRREA addressed the weaknesses regarding real property appraisals used in connection with Federally related transactions. Prior to FIRREA, appraisals for Federally related transactions and the appraisers who performed them, were, for the most part, unregulated at either the Federal or State level. During the financial crisis in the 1980's, poor quality appraisals were a contributing factor to the numerous bank and savings and loans failures. Title XI sought to address the situation.

Title XI created a unique system. As noted in GAO's report, Title XI created a complex oversight structure for real estate appraisals and appraisers that involve, private, State, and Federal entities. First, two private entities within the Appraisal Foundation establish uniform rules for real estate appraisals and set minimum criteria for certifying appraisers. Second, State regulatory agencies certify appraisers based on these criteria and regulate the industry within their State. Third, the Federal financial regulatory agencies oversees the financial institutions' use of appraisals.

Title XI charged the Appraisal Subcommittee with five legislative mandated responsibilities: First, monitor the requirements established by the States, territories, and District of Columbia and their appraiser regulatory agencies; second, monitor the requirements established by the Federal financial regulatory agencies regarding appraisal standards; third, to maintain a national registry of State-licensed and certified appraisers; fourth, monitor and review the activities of the Appraisal Foundation; fifth, transmit an annual report to Congress regarding these responsibilities.

The Appraisal Subcommittee is funded by a $25 a year fee for an appraiser to be listed on the national registry. Although the Appraisal Subcommittee has the authority to increase that fee to $50, we have maintained the registry fee at the same $25 that was es-

tablished in 1989. The annual operating budget of the Appraisal Subcommittee is currently $2.1 million. Through automation and efficiencies, the Appraisal Subcommittee has reduced its staffing from 9 employees to 7 over the 15 years of its operation, as it attempted to maintain a high level of operating effectiveness.

Perhaps the most important point I would like to make in this testimony is that generally States do a good overall job of enforcing compliance with Title XI given the resource limitations facing most States. Although some States have areas that need improvement, we have found the great majority of States are generally complaint with Title XI. Our primary tool for evaluating State compliance is a 3-year on-site review cycle. Appraisal Subcommittee staff performs an on-site review of approximately 18 States or territories a year, plus conducting several follow-up reviews. Once we have completed field reviews and formally transmitted our findings to the States, we work with the States to ensure correction of noted areas of concern. Most States address our concerns in a timely manner. Currently, the most common problematic area involves complaint investigation and resolution.

Because this area requires specialized personnel and expertise, it is one of the more complex and costly functions for State appraisal regulatory agencies. Consequently, some States are not as timely in their complaint investigation and resolution as they should be. Each year, we provide a summary of significant areas of concern identified in our field reviews in our report to Congress.

Another one of the Appraisal Subcommittee's primary responsibilities is maintenance of the registry. During the past several years, we have made the registry available via the Internet to States and to the public. We added sections reserved for the States' only access to facilitate State efforts in areas such as researching the license authority of appraisers and determining whether an appraiser is in good standing in another State. We have added automated e-mail notification to States, lenders, and other parties when appraiser credentials are revoked, suspended, or when they expire.

Senator ALLARD. Are you about ready to wrap up your comments there? Summarize quickly, and then we will submit the rest of it for the record.

Mr. FRITTS. We would offer these final comments. Some contend that the need for Federal law and Federal oversight of the appraisal regulatory system no longer exists. Given the difficulties we have experienced in achieving some level of consistency among States to better facilitate interstate lending and appraisal activities, we believe that a lack of Federal law and oversight would allow the system to become increasingly fragmented to the overall detriment of the appraisal industry.

Considering the complexity inherent in the appraisal regulatory structure, this system functions reasonably well. At 15-years-old, the appraisal regulatory system is relatively young. We expect continued adjustments and challenges as the system matures.

Thank you.

Senator ALLARD. Thank you, Mr. Fritts.

Now we will call on Mr. Clark, Real Estate Commissioner, Georgia Real Estate Commission. It is always nice to have local elected officials come and visit us here.

STATEMENT OF CHARLES CLARK
REAL ESTATE COMMISSIONER,
GEORGIA REAL ESTATE COMMISSION
ON BEHALF OF
THE GEORGIA REAL ESTATE APPRAISERS BOARD

Mr. CLARK. Thank you, Mr. Chairman, Members of the Committee. Thank you for the opportunity to present the views of the Georgia Real Estate Appraisers Board on how Congress should amend Title XI. Many other State regulators share our views.

Enacted with good intentions, Title XI today unnecessarily imposes on appraisers an unwieldy Federal regulatory superstructure not imposed on other trades or professions. We urge Congress to replace that superstructure with a traditional less costly framework, one that is more consistent with the Tenth Amendment to the Constitution.

Our board believes Title XI needs to change for three reasons. First, the Appraisal Subcommittee has met its goals. Title XI charged the Appraisal Subcommittee primarily, to see that all States regulate appraisers, and to oversee the development of the Uniform Standards of Professional Appraisal Practice. It has done so. Congress should now commend the Appraisal Subcommittee for a job well done and sunset its operations.

Second, States can provide better regulation. States have many advantages over the Federal Government in regulating appraisers. We cite but four here: The States have over a century of experience in successfully regulating businesses and professions that affect the public interest; a State's regulatory mistake has negative repercussions only Statewide, not Nationwide as does a Federal mistake; because the States investigate and discipline appraisers, they can identify and act on problems requiring regulatory attention quicker than can the Appraisal Subcommittee and the Appraisal Foundation; and the Appraisal Subcommittee and the Appraisal Foundation have chosen to make policy decisions in closed-door meetings, as they strive, directly or indirectly, to impose one-size-fits-all policies on the 55 regulatory jurisdictions and approximately 90,000 appraisers. Such secrecy is not only inappropriate, but is also counterproductive because it causes a loss of public confidence in both the decisionmakers and the regulatory process.

Our third reason for seeking change is that the negative unintended consequences of Title XI outweigh the positive results. We cite five of those here: Inhibiting the effectiveness of market controls in preventing poor appraisals; increasing the cost of regulation; requiring State governments to enforce criteria and standards developed by a private entity over which no government asserts much influence or control; denying over 90,000 appraisers the stakeholder rights in regulating their own profession that other State-regulated professions enjoy; and finally, profiteering by the Appraisal Foundation. We cite but one example here. Georgia's appraisal schools tell us that they must pay the Appraisal Foundation at least $38 each time an appraiser takes a course on appraisal standards. Under its putative Title XI authority, the Appraisal Qualifications Board, a Foundation subsidiary, forces all appraisers to take that course as a condition for becoming or remaining classified. By using its regulatory authority to enhance its financial posi-

tion, the Appraisal Foundation has misused and abused its regulatory role to reap nearly $2 million a year from appraisers. The Appraisal Foundation adopted this profiteering scheme despite the fact that the Appraisal Subcommittee has already paid it over $9 million in taxes collected from appraisers to develop appraiser criteria and appraisal standards.

Redressing these problems will require redirecting the focus of Title XI. Thus, the Georgia Board respectfully asks that Congress examine broader issues than those addressed in the GAO's report, and amend Title XI, as we have suggested in Exhibit A of the written report that we have tendered to you today.

Congress should not yield to the sirens' song that "continuing Federal regulation will lead to increased quality in real estate appraisals." Quality of work product only improves significantly through the individual practitioner's effort under the stimulus of the marketplace. State regulation can effectively establish minimum entry requirements and is removing dishonest and incompetent practitioners.

Thus, we ask Congress to end the unintended negative consequences of Title XI by sunsetting the Appraisal Subcommittee and turning appraisal regulation over to the States.

Mr. Chairman, we appreciate your Committee's time and consideration of our views.

Senator ALLARD. We will now call on Mr. Dave Bunton, Executive Vice President of the Appraisal Foundation.

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

Mr. BUNTON. Thank you, Mr. Chairman, and Members of the Committee. The Appraisal Foundation appreciates the opportunity to present its perspective at this hearing this afternoon.

Our organization serves as the private sector resource in our Nation's real estate appraiser regulatory system. By way of background, we are not a membership-based trade association, but rather a not-for-profit educational organization that serves as an umbrella group for organizations with an interest in valuation.

The appraisal profession in the United States has traditionally been somewhat fragmented. In the interest of promoting consistency and uniformity in the areas of professional standards and qualifications, eight national appraisal organizations created the Appraisal Foundation in 1987. Our mission is to promote professionalism in appraising in two important ways, first by setting the qualifications that one must meet to become an appraiser, and second, by establishing standards for how an appraisal should be performed. This is relevant because in 1989, through the enactment of Title XI of FIRREA, the Congress gave the Appraisal Foundation three specific responsibilities relating to the regulation of appraisers: First, that all appraisals performed for Federally related transactions must be in conformance with the standards promulgated by the Appraisal Standards Board of the Appraisal Foundation; second, that State-certified real estate appraisers must meet the education, experience, and continuing education requirements established by the Qualifications Board of the Appraisal Foundation; and last, the examinations used by the States to certify our real

estate appraisers must be reviewed and approved by our Appraiser Qualifications Board.

In evaluating how Title XI has performed to date, one of the most tangible measurements is to review the disciplinary action take by the States for the period of 1992 to 2002. During that time a total of 4,360 disciplinary actions were reported by the States to the Appraisal Subcommittee, and of these, over 1,250 were serious violations which resulted in the suspension, revocation, or voluntary surrendering of an appraiser's State credential.

In the event that existing that alternatives to the existing structure of Title XI are given consideration in the future, it is important to keep several factors in mind. First, the Federal Registry of Real Estate Appraisers, maintained by the Appraisal Subcommittee, currently contains over 95,000 names, accounting for individuals who hold a credential in more than one State, the total number of real estate appraisers is estimated to be approximately 80,000. We have several fine national appraisal organizations, and two of them are at the table here with us today. However, it is important to note that the majority of real estate appraisers in the United States are not affiliated with any professional appraisal organization. Accordingly, absent the current system, any type of self-regulating alternative is virtually impossible due to the fact that most appraisers are not subject to peer-review procedures.

Second, regarding the possible elimination or dilution of the Federal oversight component of Title XI in the future, it is important to remember that Title XI was enacted not as consumer protection legislation, but rather from a safety and soundness perspective to ensure the integrity of the Deposit Insurance Fund. Absent Federal oversight, States would be free to establish very low threshold levels or perhaps none at all. Without credible enforcement, there could be a detrimental impact on the safety and soundness of the Nation's lending institutions.

The current hybrid system of private sector expertise, State administration and Federal oversight ensures three things. One, minimum levels of competency. Two, it provides administrative latitude to each of the 55 States and territories. And three, it ensures overall accountability.

While we believe Title XI is generally working as intended and should remain intact, the following recommendations are offered as suggested enhancements: First, provide greater regulatory latitude for the Appraisal Subcommittee and its oversight responsibilities; second, require State-licensed appraisers to meet the qualification and examination requirements of our Appraiser Qualifications Board, as State-certified appraisers currently do; and third, to facilitate interstate commerce, reciprocity among the States should be mandated.

In conclusion, when recently confronted with concerns about the accounting profession, the Senate Banking Committee addressed the issue by increasing Federal oversight through the creation of the Public Company Accounting Oversight Board. Similarly, with the revelations about financial reporting variances at Freddie Mac, this Committee is pursuing options for greater Federal oversight of the Government Sponsored Enterprises. Fifteen years ago, when faced with a deposit insurance crisis, your colleagues opted to cre-

ate a regulatory system that includes Federal oversight of the State regulatory programs, programs that credential the individuals who determine the value of the underlying assets of our financial institutions. To dilute or remove Federal oversight at this time would be sending the wrong message at the wrong time.

Mr. Chairman, thank you for the privilege of appearing before you this afternoon, and we look forward to answering any questions that you may have.

Senator ALLARD. Thank you, Mr. Bunton.

Mr. Alan Eugene Hummel, Chief Executive Officer, Iowa Residential Appraisal Company, welcome. We always appreciate small business people showing up. I assume it is a small business.

Mr. HUMMEL. That is correct, sir.

Senator ALLARD. I know it is hard sometimes to get away from your business. Appreciate you being here.

STATEMENT OF ALAN EUGENE HUMMEL, SRA
IMMEDIATE PAST PRESIDENT, THE APPRAISAL INSTITUTE
CHIEF EXECUTIVE OFFICER,
IOWA RESIDENTIAL APPRAISAL COMPANY
ON BEHALF OF
THE APPRAISAL INSTITUTE AND THE AMERICAN SOCIETY OF FARM MANAGERS AND RURAL APPRAISERS

Mr. HUMMEL. Thanks you, Senator, and Members of the Subcommittee.

A good appraisal is important to consumers and our economy. The S&L scandal led Congress to pass FIRREA, recognizing the importance of reliable and honest appraisals in real estate financing. Today, the appraisal is being swept to the sidelines, treated as a nuisance rather than essential. Some lenders propose to bundle the appraisal with other services in cut-rate financing packages. Others intend to off-shore that function. No matter how good a computer whiz, a kid in Calcutta cannot provide the insightful evaluations on par with professional appraisers who intimately know our communities. Whether you are buying a ranch in Durango or moving to Macon, you want to know that a professional who knows the territory is involved.

So 15 years after FIRREA, how are we doing? Only 28 percent of the users we surveyed saw improvement, while fully half say that appraisal quality has declined. Before State licensing, 84 percent selected appraisers based on professional designations and experience. Now almost 90 percent of the users find State-certified appraisers less qualified than those with professional designations, yet they assign them more and more of the business.

I am afraid that the system's report card rates 5 D's and an F.

Direction is the first D; we do not have it. Our chart here depicts the regulatory structure resembling a circular perpetual motion machine. Who, individually, is responsible for setting direction? Who, in rotating bureaucratic chairmanship, is the stakeholder in charge? Is it any wonder that States routinely ignore this flailing machinery?

Disclosure is the second D, and again, we do not have it. The Appraisal Subcommittee and their civil servants hold secret meetings with neither input from nor access for professionals working in the

industry. Their tardy reports to Congress are mere financial summaries. They do not tell us what they do, only how much they are billing us. They resemble the Wizard of Oz, warning us not to look behind the curtain.

Discrimination is the third D. By favoring less-credentialed newcomers, FIRREA bizarrely discriminates against seasoned professionals, discouraging advanced career development. The professional organizations foster superior training ethics, yet with no incentive to excel, appraisers have been dropping out. Fewer than 40 percent now belong. This is like an employer snubbing college graduates to hire dropouts. Under FIRREA, ignorance is bliss.

Discipline also fails. Left alone, the States can disregard appraiser discipline as a potential Federal mandate. Take New York, which reinstated an appraiser convicted of fraudulently scamming millions. At the very time the ASC was approving New York's program, *Newsday* was reporting the State routinely neglected or dismissed complaints. We know of similar scandals throughout the country.

Duress, our fifth D, flourishes. Without effective enforcement, financiers still pressure appraisers to come up with the "right numbers" for their deals, just as they did in the freewheeling 1980's.

The ASC's worst grade is an F for Federal/State relations. The ASC has no one in charge or accountable. The Federal entity lacks practical input from the field and effective contact with States. It does nothing to foster interstate reciprocity and little toward temporary practice licensing, an appropriate Federal role.

Finally, the ASC has no real leverage to encourage State compliance. Its only inducement for the States to police bad appraisal practices have been dubbed "the atomic bomb" that would effectively blow up all Federally financed mortgages in the State. Nobody is going to use that and everybody knows it.

What happens to a 15-year-old with a flunking report card? You might pack the kid off to military school to get some discipline, but yet better, how can we help them earn some A's? Assets, enough to do the job; access to agencies' proceedings; advancement of appraisers' professional qualifications; aggressiveness in disciplining bad appraisers while protecting the independence of good ones; authority to do its job; and most of all, accountability of State and Federal oversight to the public.

Since 1935, the Appraisal Institute has advanced the standards of our industry, saving buyers, sellers, and taxpayers millions. We are now ready to work with you to craft a simple cost-effective and transparent legislative remedy so FIRREA can earn straight A's. Our system is floundering. Discipline and direction can help it make the grade.

Thank you.

Senator ALLARD. Now we will call on Mr. Eugene G. Kaczkowski, Accredited Senior Appraiser, American Appraisal Associates, Inc, here representing the American Society of Appraisers.

STATEMENT OF EUGENE G. KACZKOWSKI
PRESIDENT, AMERICAN SOCIETY OF APPRAISERS
ACCREDITED SENIOR APPRAISER,
AMERICAN APPRAISAL ASSOCIATES, INC.

Mr. KACZKOWSKI. Thank you very much, Senator. First of all, you should know that the American Society of Appraisers is a multidiscipline professional appraisal society. That is, we represent more than real estate appraisers. We also include business valuation appraisers, machinery and equipment appraisers, fine arts and antique appraisers, and gems and jewelry appraisers. About one-fifth of our membership is real estate appraisers.

The American Society of Appraisers believes that the state of the real estate appraisal profession and the profession in general is generally good, and that the enactment of FIRREA continues to be a positive force in professionalizing the Nation's real estate appraisers.

Today's real estate appraisers are far better educated, far more competent, and held to a higher standard of ethics and accountability than pre-FIRREA days.

We also believe that there is room for improvement. There are problems with Title XI; it needs to be modernized and tightened in order to correct some problems that we see. Some of them have already been addressed by other panel members.

We see seven issues or problems. First, the current membership of the Appraisal Subcommittee is drawn primarily from housing and banking interests. We think that is too narrowly drawn and lacks representation from a host of nonbanking Federal agencies that have a major stake in the integrity of real estate appraisals. These include the Department of Interior, the Department of Transportation, the IRS, the Securities and Exchange Commission, to name a few. They all have an interest in real estate appraisal issues.

Problem No. 2. Regulation of appraisers by States, territories, and the the District of Columbia has been uneven, and in some cases, even ineffectual. How to correct the problem? Give the Appraisal Subcommittee rulemaking authority.

Problem No. 3. What rulemaking powers are necessary? What we would do is have the GAO study this particular issue and determine how we can correct the problem of uneven and ineffectual regulation.

Problem No. 4. Some States continue to resist having reciprocity agreements with neighboring States and to resist issuing temporary practice permits to duly credentialed appraisers. What is the solution? Have the appraiser who is credentialed in one State be automatically credentialed in another State, in other words, have a driver's license approach.

Problem No. 5. Because Federal bank regulatory agencies have limited the mandatory application of Title XI's professional appraisal requirements to loans above $250,000 for residential property and $1 million for commercial property, the so-called de minimis rule, safety and soundness have been seriously and needlessly jeopardized. Once again, the GAO should be commissioned to analyze the effects of the de minimis rule.

Problem 6. Two years after the enactment of Title XI there were amendments, and the Appraiser Qualifications Board of the Appraisal Foundation found itself in the anomalous position of having authority to establish qualification requirements for State-certified appraisers, but not for licensed appraisers in Federally related transactions. We believe that the Appraiser Qualifications Board should have the ability to set qualifications for licensed appraisers also.

Last, because each State's appraiser licensing board currently must approve all primary and continuing education courses offered to its appraisers, hardships are imposed on those who offer the courses, appraiser societies, and regional and national education providers, who have to have these courses approved and registered by each jurisdiction. This poses an administrative hardship when the same course has to be approved 50 or more times. We say that a central clearinghouse should be established so that these courses can go to one group and have the necessary national approval. A good place to have that clearinghouse is the Appraisal Foundation.

The report that you have expands all of these issues in greater detail, but I will stand for any questions you might have.

Senator ALLARD. Thank you all for your testimony, and now we will proceed with questions from the Members on this Committee.

Mr. Kaczkowski, you have a fifth of the appraisers in your association that are also in real estate. What percentage of the total real estate appraisers do you think that represents in the country? Do you have any idea?

Mr. KACZKOWSKI. The only numbers I have are those that are provided by Mr. Bunton. I have heard those numbers before, and the thought is that——

Senator ALLARD. Four percent?

Mr. KACZKOWSKI. We have 1,000 or 1,200 appraisers out of approximately 95,000 that would be part of our organization.

Senator ALLARD. I will be darned.

Mr. KACZKOWSKI. As compared to my compadre here from the Appraisal Institute, we are a smaller group of real estate appraisers, but again, we are a multidiscipline society.

Senator ALLARD. What about the Institute?

Mr. HUMMEL. The Appraisal Institute represents approximately 24 percent of the licensed appraisers. In conjunction with the American Society of Farm Managers and Rural Appraisers, who we are testifying with, we accomplish probably about 30 percent.

Senator ALLARD. I would suppose that those who are more qualified and do the better job of appraising are likely members of both of your groups. Would that be a fair assessment?

Mr. KACZKOWSKI. We think so.

Mr. HUMMEL. That would be a fair assessment. We have shown through surveys and looking at the ASC's results of those being disciplined, we find that those that do not belong to professional organizations have a higher likelihood of being disciplined than those that do belong to professional associations.

Senator ALLARD. I see. I want to get to the fees. Mr. Hummel, you are an appraiser, so what are your fees that you pay to the Foundation and is there a separate fee to the Appraisal Subcommittee also? Give me a total of what you pay on fees.

Mr. HUMMEL. Every time I pay my license fee for every State in which I am licensed, I have a $25 tax that goes to the Appraisal Subcommittee out of that——

Senator ALLARD. So if you are, in four States, licensed then you pay $100 to the Federal agency or foundation; is that right?

Mr. HUMMEL. To the Appraisal Subcommittee, that is correct.

Senator ALLARD. Oh, the Subcommittee for each license, okay.

Mr. HUMMEL. That is correct.

Senator ALLARD. Is there any assessment from the Foundation or any other group here that you deal with?

Mr. HUMMEL. No, sir. As an individual appraiser I can voluntarily belong to the Appraisal Foundation publications, but that is voluntary.

Senator ALLARD. I understand, and then there is a fee for that publication.

Mr. HUMMEL. That is correct.

Senator ALLARD. Mr. Fritts, what have the Subcommittee's revenues been in recent years and what does it generally cost for the Subcommittee to operate? Can you share those figures with us?

Mr. FRITTS. Yes, sir. Our current budget for this year is $2.1 million. Our revenues are expected to slightly be below that expenditure amount.

Senator ALLARD. what is slightly, $100,000, $500,000?

Mr. FRITTS. About $50,000 I believe.

Senator ALLARD. So you have a $50,000——

Mr. FRITTS. Shortfall.

Senator ALLARD. You mean you collect $50,000 less than the cost of running your——

Mr. FRITTS. Than our operation and the grant to the Appraisal Foundation, is approximately $900,000 this year.

Senator ALLARD. Then you give $900,000 to the Foundation.

Mr. FRITTS. That is right, out of that $2.1 million.

Senator ALLARD. And so the $50,000, where do you make up the difference on that?

Mr. FRITTS. We have reserves of several million dollars that have been built up over the years, $5 million that is the current reserve.

Senator ALLARD. So the interest off of that reserve makes up the difference; is that the way that works or do you pull it right out of the reserve?

Mr. FRITTS. We just pull it right out of the reserve.

Senator ALLARD. Does the reserve make any money? Is it invested anywhere?

Mr. FRITTS. I believe it is with the Treasury. I do not believe it is interest bearing.

Senator ALLARD. It is not interest bearing. So the Federal Government uses that at no cost?

Mr. FRITTS. That is my understanding.

Senator ALLARD. That is interesting. You did not have a surplus this last budget year, but you have had surpluses in the past?

Mr. FRITTS. That is correct, sir.

Senator ALLARD. Let us put aside the issue of surpluses. Is it generally the Subcommittee's policy that in a single year the entire difference between revenues and its own operating expenses should be used as a grant to the Foundation?

Mr. FRITTS. No, sir, that is not how it works. Basically, the Foundation presents us a proposal in the fall of the year, which we review carefully. In past years we have sometimes approved less than that proposal, or sometimes we have approved it in its entirety. One of the GAO's recommendations was that we closely evaluate their proposal in light of their review, and if possible and appropriate, go into our reserves to help fund that request. This request last year, we did fully fund their request at $900,000, and that will result, at least in our budgetary process, a slight shortfall.

Senator ALLARD. Do you expect the shortfall to increase in future years?

Mr. FRITTS. If we do not increase the fee, the $25 fee, which has been the same since 1989, that is entirely possible. Yet, with our reserve that we have there, that is still some time away.

Senator ALLARD. Senator Reed.

Senator REED. Thank you very much, Mr. Chairman.

Thank you, gentlemen, for your excellent testimony.

One of the basic questions here is whether this authority and responsibility should devolve back to the States. Mr. Wood, in your study, GAO study, you found that the biggest constraint on all the regulatory bodies was a lack of funding I believe. Is that accurate?

Mr. WOOD. That is what the States reported was their biggest impediment, a lack of resources.

Senator REED. Which raises a question of not only the willingness but also the capacity of States to take up this extra—do you have any comments in terms of that from your review about the capacity of the States to do this work, not just one or two States that may be well prepared, but across the board?

Mr. WOOD. In terms of the capacity to actually do the job the Title requires them to do, I would say the Subcommittee is probably in a better position to answer you because they do annual reviews of the States on a rotating basis. But there are some data in our report that amply lays out shortfalls they are experiencing.

Senator REED. Mr. Fritts, let me raise the question with you about the capacity of not individual States, which I am sure they are well prepared, but the range of States.

Mr. FRITTS. Yes, sir. We are certainly concerned about the current budgetary issues, and that is one thing we are monitoring when we are doing our reviews. Many States are under budgetary pressures. We have found, however, over the 15 years, that States have done a very effective job. Our report results show that. Out of all the States that we have, we put States in three tiers of classification as to their compliance, and there are only four States and territories that meet less than really what we consider reasonable compliance and reasonable quality of their programs. That is our current statistic.

Senator REED. So that in your view, they do have the capacity?

Mr. FRITTS. Based on past experience, we believe they do.

Senator REED. Let me ask another question, Mr. Fritts. Apparently, the only real sanction you have is decertification of a State.

Mr. FRITTS. That is right, sir. I will say it is a very powerful sanction, and just the threat of it we believe is a very powerful inducement. We have I think a good cooperative relationship with

the States, and our experience is that when we find problems, the States correct them generally in a timely fashion.

Senator REED. So you do not believe there is a need for a range of sanctions or authorities, that this decertification is adequate and sufficient and not too much?

Mr. FRITTS. I think our experience shows that it has been adequate up to this point.

Senator REED. Mr. Clark, you clearly have espoused the notion that Title XI should be dispensed with and these duties devolve back to the States. Are there any recommendations short of that that you would support, any other fixes to the system, or your position is it so broken and it has to be done away with?

Mr. CLARK. Senator, we think it is broken, but we would not recommend doing away with all of it. Our proposal specifically identifies the things that we would do, and while we would sunset the Appraisal Subcommittee and have the States to handle all the education and experience requirements and the examination requirements, there are things in Title XI that we think are important to retain, simplified to some degree.

For example, we think that we should authorize lenders to use any classified appraiser they choose so long as that appraiser is classified in a State. So, for example, a lender who is making loans across the country on large buildings, for example, might hire one appraiser who happens to be licensed in one State, and that appraiser could do work wherever the lender wanted them to do, to get over this hurdle of fighting between the States about whether you can go across a State line or not. We think that Title XI should require that lenders utilize appraisers classified by State regulatory agencies in all Federally related transactions. That assures that every State will have an entity to license and certify appraisers. If Title XI did not require that, some State might decided, hey, we just do not want to do this. So it would be a stimulus to see that it is done.

We think that all appraisals should be conducted on Federally related transactions in accordance with USPAP, and we see an important role for the Standards Board of the Appraisal Foundation to continue to play in establishing those standards. We think they should be working more directly with the financial institutions to accomplish that, rather than being paid by appraisers through the current payment system. So we think there are a number of things in Title XI that are very valuable that should remain.

We are concerned that the regulation should go back to the States.

Senator REED. Thank you, Mr. Clark, thank you.

My time has expired. Mr. Chairman, I assume that the witnesses will be available for written questions?

Senator ALLARD. Absolutely. In fact, if you have other questions you will not get a chance to ask here, we will have you send those to the panel. And then if the panel would respond within 10 days, we would certainly appreciate it. It would be very helpful.

Senator REED. Thank you, Mr. Chairman.

Senator ALLARD. Senator Miller.

Senator MILLER. Thank you, Mr. Chairman, and thank the panel.

Let me ask my first question of Mr. Wood. Do you think the fees for training and the qualifications for licensure are appropriate and consistent across the country?

Mr. WOOD. The fees for licensing of course are set by each State. We did not collect that information. However, we did get information from the Subcommittee which maintains that. There is quite a bit of variation, and it varies depending on what category of appraiser we are talking about, whether it is licensed, a certified residential, or a certified general. There is a good deal of variation in terms of the time period that a license covers. I can just give you a flavor of some of the ranges that we found.

Senator MILLER. I would think the answer is no though, is it not? Your answer would be no, they are not consistent.

Mr. WOOD. That is correct, it is not consistent across the country.

Senator MILLER. How about the word that I used also, "appropriate?"

Mr. WOOD. I guess appropriate, you know, in——

Senator MILLER. To the job.

Mr. WOOD. In passing Title XI the Congress left this up to the State, so my response would be if the State finds it appropriate, then I find it appropriate.

Senator MILLER. Do you think they are appropriate and consistent as compared with other State-licensed professional groups as far as your information is concerned?

Mr. WOOD. We did not compare the appraisers to any other professional groups.

Senator MILLER. You got a guess?

Mr. WOOD. I really do not. I am sorry.

Senator MILLER. Who is responsible for the oversight of the fee structure?

Mr. WOOD. Again, for licensed appraisers, it is the States. And actually the States also set their fees for certification. The Subcommittee can review them, but it has no real power over them.

Senator MILLER. Mr. Fritts, as we all know, Title XI was designed to protect the Federal Deposit Insurance Funds from faulty and fraudulent appraisals. On a scale of 1 to 10, is there still a need to protect the Deposit Insurance Funds?

Mr. FRITTS. I believe there is a need. The scale, of course, being a full-time employee of the Federal Deposit Insurance Corporation for 28 years, I feel pretty strongly about that, the need to protect depositors. So, I guess I would rate that as a 10.

Senator MILLER. Let me ask this question of Commissioner Clark. From your knowledge of this, and I know it is considerable, what other States that you know of agree with your view on amending Title XI, to the extent that you would like to see it amended?

Mr. CLARK. In the GAO report, there were some numbers that we found interesting, and that was, I believe, if I recall them correctly, there were 15 States that felt like the Appraisal Subcommittee needed to continue. There were 23 States, I believe, that sided with our view, and then 15 States that were on the fence on that particular issue.

I suspect there has been some shift in that. This last year, for example, the Appraisal Qualifications Board doubled the entry re-

quirements for licensed and certified appraisers beginning in the year 2008, and I suspect there will be some negative reaction to that.

In terms of the States that I am aware of, people that I have personally spoken to, regulators in the following States tell me that they support our position—the States of Washington, Oregon, Utah, Wyoming, Colorado, Kansas, Texas, Arkansas, Mississippi, Alabama, Florida, South Carolina, North Carolina, Kentucky, Vermont and Maine.

I cite all of those States because I think they represent a pretty broad spectrum of the types of States that we are dealing with, smaller States that will have more difficulty in funding their operations, as well as larger States who are not confronted with that difficulty, but regulators in all of those States have indicated to me personally that they support our general position.

Senator MILLER. I like leaving things up to the States, as you can probably imagine, but how would you—well, my time is up. Can I go ahead and ask this question or I can get it in the next round.

Senator ALLARD. Go ahead. We will have another round.

Senator MILLER. How would you ensure consistency across the States for programs if the Federal Government gave up its role or is there a need for consistency?

Mr. CLARK. I think there is a need for consistency, but I think that takes place naturally. If you look at all of the other professions that are regulated and move from State to State, they have generally consistent requirements. Doctors and lawyers, despite the fact that they were all developed in 50 different States, have come to essentially the same body of knowledge.

I would imagine that suppose we just stopped tomorrow and pulled out Title XI altogether, I would imagine that all of the States would keep in place the current requirements. There would be some experimenting with that, and there should be some experimenting with that. As new ideas come along, you want to try those and operate differently, and that is one of the values of State regulation. If an individual State can try something new, if it works, everybody adopts it. If it does not work, nobody else is hurt by it. But I would fully expect the general requirements to stay approximately where they are now.

Senator MILLER. Thank you.

Senator ALLARD. Mr. Clark, I am going to follow up on reciprocity. I belong to a profession, and we do national testing.

Mr. CLARK. Yes, sir.

Senator ALLARD. When you graduate from school, you take a national test, and then the States decide whether they are going to accept the national test. In addition to that, there are orals that we take, and then, as a veterinarian, we pay the fees for the tests. Also, in our profession, it is usually decided at the State level, the State decides on whether or not they want to have reciprocity with their neighbors.

Do you want to move toward national testing or mandates from the Federal Government, setting down some minimum standards on the States? I am trying to figure out how we can make this reciprocity work.

Mr. CLARK. I do not want national testing. I think it is important to have the flexibility of the States administering their own exams, and I think that is a very important thing to retain. However, I certainly do believe in reciprocity, and one of our provisions, the Georgia Board's provisions, would assure that reciprocity by saying that if an individual has an appraiser classification in Colorado, then he can be hired to work in Michigan, he can be hired to work in Georgia, California, anywhere, as long as he is classified in that State. That would be the stimulus from the Federal Government to assure the ability to work Nationwide.

Senator ALLARD. But all States do not require licensing.

Mr. CLARK. It is my understanding that the Appraisal Subcommittee has set up licensing Nationwide. And if you are going to appraise in a Federally related transaction, you must be certified or licensed.

Senator ALLARD. But there are some appraisers out there that would not be licensed necessarily because they would not be dealing with a Federal program; is that right?

Mr. CLARK. That is correct in some States. In many States, all appraisers are required to be classified.

Senator ALLARD. I see.

Mr. Fritts, are the Subcommittee meetings open to the public?

Mr. FRITTS. As far as I am concerned, they are.

Senator ALLARD. I know you may be concerned and want it to happen, but are they open to the public?

[Laughter.]

Mr. FRITTS. There is no Government sunshine notices for the meetings. We meet monthly. Since I have been chairman, this issue has come up, invited a number of the members in the appraisal industry, I think maybe even some people here at this table, to attend our meetings, and I certainly would not voice concern about moving toward that.

Senator ALLARD. Are public notices put out so the public knows and the press knows that you have these meetings?

Mr. FRITTS. We could put it on our website.

I will say the only part that we probably would not want public is where we go over the reviews of each State's evaluation.

Senator ALLARD. You mean the State's evaluation is not made public? These are public officials.

Mr. FRITTS. Yes, the State report is, but in the discussion, the discussion of the report and the proper——

Senator ALLARD. Because it involves individuals; is that right?

Mr. FRITTS. It involves individuals, and it is deliberative relative to what our responses will be.

Senator ALLARD. I think that is understandable, but it seems to me like you could advertise them, like you say, put them on the Internet or something so people know that——

Mr. FRITTS. I have invited a number of people to come to our meetings. I certainly have no problem with it. None have ever taken me up on that offer.

Senator ALLARD. If you have a way of putting a public notice out there, I would encourage you to do it. I think it would help.

Now, let me see, the GAO report indicates that most mortgage fraud problems occur in States where licensing is voluntary. Mr.

Wood, would you please elaborate, and do you believe we should move to a mandatory system?

Mr. WOOD. First of all, the data are very anecdotal, and I think that is one of the areas that I would say, coming out of our work, deserves further study. No one really knows, for example, how many mortgage transactions are even covered by Title XI; in other words, how many are Federally related. So, I would say that deserves more study.

Senator ALLARD. Any other members on the panel that would like to comment on having voluntary licensing in some States, and do you think we should move toward a mandatory system?

Mr. HUMMEL. The mandatory system concerns me under our current structure. If we had a mandatory system in which we had the Appraisal Subcommittee overseeing everything, I would have concerns only because the Appraisal Subcommittee has not been properly held accountable or provided the authority, quite honestly, to do their job. And so if we had mandatory licensing in which all of a sudden every time I did an estate appraisal versus a mortgage appraisal, and I was held under the Appraisal Subcommittee's thumb, I would be uncomfortable, and I think the State would also.

Until that is remedied, I would not suggest mandatory licensing.

Senator ALLARD. Senator Reed.

Senator REED. Thank you very much, Mr. Chairman.

Mr. Bunton, in your testimony, you pointed to the disciplinary actions of the States between 1992 and 2002 as a measure of how well Title XI is doing. Do you have comparative data prior to the adoption of Title XI or prior to 1992 so that we can put that in context?

Mr. BUNTON. I do not, but it is important to note that prior to 1989, I believe there were only three States that were regulating appraisers. This was the catalyst that changed the landscape as far as regulating appraisers. Before that, it was if you belonged to a professional society, you had peer review. So there really is no data before this. I think Nebraska, Louisiana, and perhaps Florida were the only three that were regulating appraisers in any way.

Senator REED. Given this information that there are active States that are identifying and disciplining appraisers who are violating rules and regulations, I mean, one of the real concerns that we have is that there are, as there is in every line of endeavor, people who just do not follow the rules. Is it your opinion the States are doing an adequate job of enforcing their regulations or this number that you cited is good, but it is just the tip of the iceberg?

Mr. BUNTON. I think the GAO at one of the tables in their report gives a State-by-State breakdown. And if you look at that and the various disciplinary options available to each State, you can see there is a a philosophy with each State board. Certain States will give an awful lot of education instead of fines or suspensions. Others are very quick to suspend. That is one of the problems we have. We do not really have consistency in enforcement.

Senator REED. Again, I guess in the context of a Federal superstructure, at least, are you urging more consistency in enforcement, and this is an example of where——

Mr. BUNTON. Very much so. In fact, just from our organization's point of view, we put together a compilation of court cases and ad-

ministrative rulings. We have done two editions now and disseminated it to the States just to show States how similar situations are being handled in neighboring jurisdictions.

Senator REED. Thank you.

Mr. Hummel, thank you again for your testimony. Do you have any comments on this line of inquiry about the capacity of the States, financially, to take a more prominent role? I think Mr. Clark was quite eloquent in saying we do not want all of Title XI gone, but we want the States to have a more prominent role. Also the issue of are the States actively playing that role today?

Mr. HUMMEL. The States, it varies across the board, and I will use an example, the State of Iowa. The funds that are collected from the license fee go into the general fund, not into that specifically for enforcement, and because of that, they are woefully lacking, not that they do not try. There are very good individuals on those State boards, the Executive Committee is very good, but they do not have the funds to do the prosecution. Many times they choose not to do the prosecution because it is just too costly.

We have other States that actually have attorneys that are, by nature, part-time to that particular board, and they are charged for their pro rata share, and the attorneys are not interested in going forward. So it is not always a matter of money, but sometimes a practicality of having the administrative staff available.

Senator ALLARD. Thank you.

Mr. Kaczkowski, your comments.

Mr. KACZKOWSKI. As I mentioned earlier, the regulation, as we see it, has been uneven, inconsistent, and something can be done about it. Give the Appraisal Subcommittee a rulemaking authority to settle some of these issues on just what needs to be done. How do you get uniformity? Some oversight board needs to provide that impetus.

We have not seen uniformity in the States on the issue of reciprocity, much less the driver's license idea, and also, as I mentioned, on the education issue, where all of the States seem to want to approve the same course independently. There is no need for that. There is a better way of doing it, and that is why I am a little bit reluctant to provide too much power, if you will, to individual States because then for appraisers who are not local, who are not operating only in a single State, it becomes a relative administrative nightmare for them to do their job.

For example, we operate internationally in our firm. In trying to comply with State licensing or certification—we do not have licensed appraisers, we have only certified general appraisers—it is very, very difficult to have an appraiser who is certified in 15 or 20 States.

Senator REED. Thank you very much.

Thank you, gentlemen.

Senator ALLARD. Senator Miller.

Senator MILLER. Let me ask this question of Mr. Wood and Mr. Fritts.

Does Title XI bring Federal protection to real estate appraisals, especially now when so much appraisal fraud, we are told, is increasing?

Mr. WOOD. We do not have any data before—we cannot compare before and after Title XI.

Senator MILLER. We do not know?

Mr. WOOD. So, I could not say on that basis.

Senator MILLER. Do you know, Mr. Fritts?

Mr. FRITTS. I cannot say with a degree of certainty. I would say the fact that over 1,100 appraisers have been disciplined significantly in the last 13 years indicates that Title XI and the system that it built does have some good checks and balances and has improved the quality of the industry over that time period.

Senator MILLER. I guess this is a question for both of you, also, and if anybody wants to jump in and answer it and say what you think, let me know, also.

What kind of data is out there on the scope of complaints about appraisals per appraiser?

Mr. WOOD. Actually, we have a table in our report, that I think was referred to earlier, that shows the different complaints by State. There is a total of about 4,000 or so complaints in there.

Senator MILLER. Is that what you were going to refer to, Mr. Clark?

Mr. CLARK. No, sir. I would point out something a little different in that line. One of the things we hope the GAO report would do would identify exactly how many transactions go on that require appraisals, and apparently that was beyond the scope of the report.

But two snapshots I think are important in this. The Georgia Department of Banking Finance tells us that in the year 2000, banks in the State—that is all banks, both Federally related and others—made 270,560 loans that required appraisals.

Senator MILLER. How many?

Mr. CLARK. It was 270,560 in the year 2000. Our board has received 83 complaints out of those 270,000. Fannie Mae filed 860 complaints with State agencies in I think it was 2002 to 2003 or 2001 to 2002 out of 11,700,000 mortgages they hold. So, if there were only 860 appraisals that they had concerns with, that is less than one-ten-thousandth of 1 percent. And I think that says that appraisers are generally doing a good job. I am not sure that the problem is quite as large as we may think it is. Clearly, we still have a flipping problem, but I think the States are acting on that, as it says in the report.

Senator ALLARD. Mr. Fritts.

Mr. FRITTS. I agree that the industry, by and large, does a good job and that the problems of seriously bad appraisals is a relatively small minority, but any bad appraisal has serious consequences.

Senator ALLARD. Mr. Hummel.

Mr. HUMMEL. The statistics are a wonderful thing, but we have to be very careful because Fannie Mae did, in fact, send in 870 complaints, and then they stopped because they found that, out of those 870 complaints, such a minuscule amount were actually being handled by the State boards. They found that the State boards would not communicate with them as to what disposition those complaints had, either that or they would ask for information or personal testimony, so that the infrastructure of handling those complaints at the State level was so frustrating that they stopped turning them in.

Senator MILLER. While you are talking, let me follow up and ask you if you care to elaborate any more about there being enough funding and resources at the State level to meet the requirements of Title XI.

Mr. HUMMEL. In fact, I believe that there is not sufficient funding.

Senator MILLER. What can be done?

Mr. HUMMEL. Pardon?

Senator MILLER. That is what I want you to elaborate on. I gather that, but if not, and you believe there is not, what can be done? What would you suggest?

Mr. HUMMEL. I would suggest——

Senator MILLER. I liked your idea of, a while ago, moving to Macon. If you were talking about moving to Macon, Georgia, that would be a very good idea.

[Laughter.]

Mr. HUMMEL. And while I was in Macon, what I would do is ask Congress to look at FIRREA and, importantly, two things I would ask them to look at is, one, the Appraisal Subcommittee does have certain influences. I talked about, you know, basically we have given them a tablet of paper and an atomic bomb, and that is all they have to enforce the rules with.

They need something in between, and they need to be held accountable by Congress to making certain that the State boards are properly functioning. With $5 million in the kitty right now, it is possible that there might be some way that they can help with the enforcement—again, given proper oversight and then give them the authority to go in and the tools to make certain States are using their enforcement powers.

Second, one thing that we could do, and the change would be repealing Section 1122 of FIRREA. Section 1122 is bizarrely called "the Antidiscrimination Clause," and what it does is it discriminates against individuals of higher-level education and training, and states, you know, that they should not be the ones chosen to do the services. We need to recognize and encourage the use of designated appraisers with qualifications beyond the certified and licensed levels.

Senator ALLARD. Senator Miller, we are going to have another round with the Committee. I would make it the last round, if that is all right with the Senators here.

I have one question. I just want to follow up on the issue that Senator Sarbanes brought up and get your response to that.

The Committee has heard a number of concerns with seller-assisted downpayment programs, in which the seller makes a contribution to a charitable organization, which then makes a gift to the purchaser for a downpayment and closing costs. Apparently, this is a problem in Maryland, which Senator Sarbanes represents. According to information I have received, many properties sold through these programs are financed for more than their market value.

Mr. Clark, have you seen this problem in Georgia?

Mr. CLARK. Yes, sir. We have had two or three cases of that were brought to the attention of the board, and the board has disciplined the appraisers involved in those situations.

Senator ALLARD. And you think you have the situation well under control in Georgia?

Mr. CLARK. In the sense that we could respond to it when we identify it, but I think that there is a bigger problem there, and that is the banking standards that would allow them to make loans when they recognize these gift situations occurring. I think there is some responsibility for the bank there, as opposed to necessarily the appraiser. We just happen to know of two or three cases in Georgia where the appraiser obviously inflated the value.

Senator ALLARD. I see.

Mr. Hummel and Mr. Kaczkowski, how can we ensure that appraisals are not inflated in such programs? Maybe you two could respond.

Mr. HUMMEL. The situations I have seen that occur, quite honestly, we had individual appraisers that were incompetent. They did not understand the proper methodology to analyze that particular property and the financing inherent in it. And so one of the solutions, again, is to recognize that we should not be solely selecting the minimally qualified licensed and certified appraiser, but giving some type of endorsement and encouragement to making certain that the appraiser who is best qualified does that particular service.

Senator ALLARD. You believe it is a matter of ignorance and not a matter of intentionally trying to be part of a program to defraud?

Mr. HUMMEL. There are certain individuals out there, without question, that choose to commit fraud. There are others that, again, because of their incompetence, provide false appraisals.

Senator ALLARD. So what can we do to ensure that it is not inflated?

Mr. HUMMEL. Again, I would suggest the repealing of Section 1122 of FIRREA because so many lenders have read that and said, "What this says is that I should not look at the highest qualified. I am supposed to go to simply the certified or licensed individual, even if I know there are individuals out there with higher qualifications and education that would competently perform this assignment for me." My suggestion would be to repeal Section 1122 of FIRREA.

Senator ALLARD. Mr. Kaczkowski, do you want to add anything?

Mr. KACZKOWSKI. Yes, there is one issue, and that involves the de minimis rule.

Senator ALLARD. Yes.

Mr. KACZKOWSKI. That says that appraisals are required for a residential property over $250,000. So, if you want to cheat, I suppose you should cheat on those properties that are under $250,000.

Senator ALLARD. Or less than $1 million on commercial property; is that——

Mr. KACZKOWSKI. A million dollars on commercial, that is correct. So that is one way of doing it. Other than having competent and conscientious appraisers who are aware of the situation report these unethical and criminal acts, I do not know if there is any systematic way of doing it.

Certainly, a competent appraiser who has access to selling data would know that there would be, let us say, unusual buying and selling activity. There are certain rules that require the appraiser

to consider all sales that have been made of a property over a certain period of time. If that information is reported properly, competently, that is part of an appraiser's responsibility. If you choose not to accept that responsibility, and lie and cheat, the only way that you are going to be found out is if someone will report you. I do not know how you legislate that.

Senator ALLARD. Would a credit score from the bank reflect that? Maybe in some instances.

Mr. KACZKOWSKI. I do not, offhand, see how that would.

Senator ALLARD. I mean, if you have one individual scoring, doing a lot of loans and whatnot, the credit score that is the only place I could think of where it might show up.

Senator Reed.

Senator REED. I have no questions.

Senator ALLARD. Senator Miller.

Senator MILLER. This is my last one, and I do not mean to start this hearing all over again, but let me ask this of each one of you, just go down the line and start with Mr. Wood all the way through.

I know you could speak a long time on it, as you already have and with your testimony, but I would suggest you try to respond somewhere between the answer "it would be a disaster or not anything." And my question is what would be wrong with the Federal Government allowing States to regulate appraisers in the same way they do other professions?

You do not have to answer that the way I suggested, but in your own words. But what I was pointing out was somewhere in between those two extremes.

Mr. WOOD. The only experience that I can point to is, of course, pre-FIRREA, where it was clearly seen to be a mistake or a weakness. Whether that disaster would repeat itself, I do not know, but that is certainly what we are trying to avoid.

Mr. FRITTS. I would echo Mr. Woods' comments. My own personal experience, having closed many banks and thrifts, I can speak personally to the fact that the poor quality of the appraisal products pre-FIRREA clearly had a contributory factor in the result of all of those failures, not all of them, but many of them.

Senator MILLER. You just cannot trust those States?

Mr. FRITTS. Oh, I think we can trust those States. I think the States do a good job. Pre-FIRREA, most States did not regulate the appraisal industry.

Senator MILLER. Mr. Clark.

Mr. CLARK. I am generally in agreement with Mr. Fritts on this issue. I think the States can do it, and should do it, but I think there is a need for Title XI to say that banks are going to have to use a State-licensed or certified appraisal. That will force all States to see to it that they do it.

Mr. BUNTON. The States can do it, but it is the Federal oversight that is the glue that holds this all together.

We do not have—Mr. Clark mentioned the medical community or the legal profession—we do not have a bar association or an AMA. Most appraisers, we pointed out, do not belong to an organization. And before FIRREA, only three States were licensing and certifying. I think that it would go in 55 different directions.

Mr. HUMMEL. From personal experience, I was at one time licensed in five different States. I chose not to be licensed in five different States because, even as an instructor of appraisal education, I was still required to sit five different times for the same course because I carried licenses in five different States.

I believe that States can do good work within their boundaries, but we must have the Federal oversight to pull it all together, and, again, that Federal oversight being properly accountable and properly funded.

Mr. KACZKOWSKI. I would not like the appraisal profession to be lumped in with the accounting profession because of recent events.

[Laughter.]

But we have seen fit to put together a Public Company Accounting Oversight Board, and it seems to me that, just by analogy, what we have going for us right now is a pretty good thing, that we do need some coordinating and oversight board for the appraisal profession.

And the one other thing I cannot quite reconcile in my own mind right now is that Title XI relates to Federal interest. I am not clear how the States would protect the Federal interest without Title XI.

Senator MILLER. Do you agree with that, Mr. Clark?

Mr. CLARK. No, sir. I think it is very clear how Title XI can protect the Federal interest, but still allow the States to do the regulation. That is why I outlined the things that I think Title XI needs to remain in. It needs to have a clear statement that the States will do this regulation. It needs to have a clear statement that if you have a license in one State, you can appraise in any State. Those are things I think are very appropriate at the Federal level.

But in terms of establishing the minimum requirements, in terms of regulating the persons involved, that should be a State function.

Senator MILLER. Does anyone else want to add anything to this discussion?

[No response.]

Thank you very much. I thank the panel very much.

Senator ALLARD. Yes, thank you. I would like to thank all of you for taking time from your jobs to be here and discuss this important issue with the Subcommittee.

At this time, I would ask unanimous consent to enter into the record a letter from Stewart Leach, who is the Program Administrator of the Colorado Board of Real Estate Appraisers.

Senator ALLARD. The record will be held open for 10 days should any other Member wish to submit a statement or questions. I would ask that the witnesses promptly answer any questions that may be submitted.

Again, I want to thank you all for coming, and this hearing is adjourned.

[Whereupon, at 4:03 p.m., the hearing was adjourned.]

[Prepared statements, response to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF DAVID G. WOOD

DIRECTOR, FINANCIAL MARKETS AND COMMUNITY INVESTMENT
U.S. GENERAL ACCOUNTING OFFICE

MARCH 24, 2004

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to be here today to discuss our report on Federal oversight of the real estate appraisal industry.[1] In response to concerns that faulty and fraudulent appraisals played a major role in the savings and loans crisis of the 1980's, Congress enacted Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Among other things, Title XI requires that real estate appraisals used in connection with federally related transactions be performed in writing, in accordance with uniform professional standards, and by individuals whose competency has been demonstrated and whose professional conduct is subject to effective supervision.[2]

My statement today, which is based on our May 2003 report, discusses (1) the specific responsibilities of the entities that comprise the Title XI oversight structure, (2) factors which these entities identified as potential impediments to carrying out their Title XI responsibilities; and (3) concerns expressed by the entities and industry participants about the effectiveness of the existing regulatory structure. In preparing our report, we reviewed FIRREA and its legislative history; interviewed officials from the entities involved in the Title XI regulatory structure; and surveyed appraiser regulatory agencies in the 50 States, the District of Columbia, and U.S. territories.[3] Additionally, we met with officials and representatives of Fannie Mae and Freddie Mac, Government Sponsored Enterprises (GSE's) that establish standards for appraisals associated with mortgages they purchase; the Department of Housing and Urban Development (HUD), which establishes appraisal requirements for its insured mortgages; trade groups representing appraisers and mortgage lenders; appraiser education providers; and academic experts.

In summary, we found the following:

- Title XI created a complex regulatory system that relies upon the actions of private, State, and Federal entities to help assure the quality of appraisals and the qualifications of appraisers used in federally related transactions.
- Two private entities—the Appraisal Standards Board and Appraiser Qualifications Board—respectively establish (1) uniform rules for preparing and reporting real estate appraisals and (2) minimum qualification criteria for certified real estate appraisers. Certified real estate appraisers are one of the two categories of appraisers listed in Title XI, the other being licensed real estate appraisers.
- States establish the minimum qualification criteria for licensed real estate appraisers. In addition, States (1) implement the certification and licensing of all real estate appraisers and (2) monitor and supervise compliance with appraisal standards and requirements. The States and territories have established structures typically consisting of a State regulatory agency coupled with a board or commission to establish education and experience requirements, license and certify appraisers, and monitor and enforce appraiser compliance.
- The Board of Governors of the Federal Reserve System (FRS), Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), Office of Thrift Supervision (OTS), and National Credit Union Administration (NCUA)—hereinafter referred to as "the Federal financial institution regulators"—are responsible for ensuring that real estate appraisals used by federally insured depository institutions comply with Title XI. The regulators have (1) adopted rules and policies specifying transactions for which regulated financial institutions are required to obtain an appraisal by a certified or licensed appraiser, (2) developed examination procedures to ensure that regulated financial institutions are in compliance with Title XI, and (3) appointed agency representatives to the Appraisal Subcommittee.

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[1] U.S. General Accounting Office, Regulatory Programs: Opportunities to Enhance Oversight of the Real Estate Appraisal Industry, GAO–03–404 (Washington, DC: May 14, 2003).

[2] As defined in Title XI, federally related transactions are real estate transactions involving financial institutions regulated by the Federal Government. These include banks, thrifts, and credit unions. Real estate transactions of mortgage bankers, brokers, pension funds, and insurance companies are not included.

[3] The territories included in our survey are Guam, Northern Mariana Islands, Puerto Rico, and the Virgin Islands. The only other U.S. territory—American Samoa—did not have a regulatory oversight structure for appraisers. We received responses from all but one survey recipient (U.S. Virgin Islands). In this testimony, the term "States and territories" refers to the 50 States, the District of Columbia, Guam, the Northern Mariana Islands, and Puerto Rico.

- The Appraisal Subcommittee, which was created by Title XI, is responsible for monitoring the implementation of Title XI by all parties—private, State, and Federal. The Subcommittee monitors the efforts of the Federal financial institution regulators in developing and adopting appraisal-related regulations and policies, conducts periodic reviews of each State's licensing and certification program, monitors and reviews the Appraisal Foundation, and provides grants to the Foundation to support the Title XI-related activities of its two boards—Appraisal Standards Board and Appraiser Qualifications Board.

Entities involved in the Title XI regulatory structure described a number of factors that they believe constrain their ability to perform more effectively and efficiently. For example, officials of the Appraisal Standards Board and the Appraiser Qualifications Board told us that insufficient Federal grant funding may impede their ability in the future to ensure that standards and qualifications evolve with changing conditions, such as how to appraise contaminated or polluted properties. State appraiser agencies—which are funded at the State level—reported resource limitations as the primary impediment in carrying out their oversight responsibilities. For example, of the 54 States and territories that responded to our survey, 26 reported that the current number of investigators was insufficient for meeting the States' regulatory responsibilities, 37 cited a need for increasing the staff directed at investigations, and 22 cited a need for more resources to support litigation. The five Federal financial institution regulators reported no major impediments to carrying out their Title XI responsibilities. The Appraisal Subcommittee reported that rulemaking authority and additional authority to ensure State compliance with Title XI could facilitate its monitoring of State compliance with Title XI. Subcommittee officials stated that the only mechanism available under Title XI for effecting State compliance is to decertify a State, which would prohibit all licensed or certified appraisers from that State from performing appraisals in conjunction with federally related transactions and have a devastating effect on the real estate markets and financial institutions within that State. However, the Appraisal Subcommittee stated that it has always been able to achieve States' compliance under the current enforcement and regulatory structure.

Officials of the regulatory agencies, appraiser trade groups, education providers, the mortgage industry, HUD, and the GSE's voiced concerns about Title XI's regulatory structure. However, we noted no clear consensus on the need for or impact of possible changes. Some industry participants stated that a growing number of real estate transactions, such as those placed through mortgage brokers and those falling below a dollar threshold set by the Federal financial institution regulators, are not universally subject to Title XI appraisal requirements. In addition, some industry participants cited concerns with the lack of a national qualification criteria for the licensed real estate appraiser category. Education providers and appraiser trade groups expressed concerns about the Appraiser Qualifications Board's fees and requirements for instructor certification and course approval. Federal and State regulatory officials expressed concern about the apparent reluctance of lending institutions to make referrals or complaints regarding questionable appraisals they identify. HUD and GSE officials expressed concerns about a lack of consistent and effective enforcement actions by the States on referred cases and the adequacy of the Appraisal Subcommittee's oversight of State programs.

We made four recommendations to the Appraisal Subcommittee intended to enhance the effectiveness of the existing regulatory structure. As of March 17, 2004, the Appraisal Subcommittee reported that it has taken action on three of the recommendations: to (1) develop and apply consistent criteria for determining and reporting States' compliance with Title XI; (2) explore options, including drawing on its surplus, for addressing Appraisal Foundation grant shortfalls; and (3) provide nonfinancial assistance to aid the States in carrying out their Title XI responsibilities. The Appraisal Subcommittee reported that it attempted but has not been successful regarding our fourth recommendation, which was to coordinate with Fannie Mae, Freddie Mac, and HUD to improve the process of referring problem appraisals to State appraiser agencies for enforcement.

Background

An appraisal is an opinion of the value of a property as of a specific date. Appraisers generally consider a property's value from three points of view—cost, income, and comparable sales—and determine an estimated value based upon weighing the three valuation methods. The comparable sales approach, which compares and contrasts the property under appraisal with recent offerings and sales of similar property, is usually considered most appropriate for estimating the value of residential real estate.

The primary role of appraisals in the mortgage loan underwriting process is to provide evidence that the collateral value of property is sufficient to avoid losses on loans if the borrower is unable to repay the loan. Consumers often mistakenly assume that appraisals are intended to validate the purchase price of the property in question. Furthermore, appraisals are sometimes confused with home inspections, which are intended to warn consumers about serious defects in the home being purchased that should be repaired. In a loan transaction, the lender rather than the borrower engages the appraiser, and this usually occurs after the borrower has agreed to purchase the property.

The primary purpose of the appraisal reforms contained in Title XI was to assist in protecting the Federal deposit insurance funds—and, by extension, mortgage lenders—from avoidable losses. Officials of the Federal financial institution regulators noted that faulty and fraudulent real estate appraisals have been associated with losses incurred by federally insured financial institutions and have resulted in financial harm to individual consumers. However, all of the regulators stated that real estate appraisals have not been a major factor in the failure of depository institutions since the passage of Title XI.

Title XI Created a Complex Oversight Structure

Private, State, and Federal entities have responsibilities under the Title XI regulatory structure. Private entities—the Appraisal Standards Board (ASB) and the Appraiser Qualifications Board (AQB)—establish minimum standards for the development and reporting of real estate appraisals and minimum qualification criteria for certified appraisers. States are responsible for certifying appraisers, using education and experience requirements that, at minimum, meet AQB criteria, and for enforcing compliance with appraisal standards. States may also license appraisers using State-established licensing criteria. (For those States that had both, experience and education requirements for certified real estate appraisers exceeded those for licensed real estate appraisers.) The Federal financial institution regulators establish appraisal requirements for the insured depository institutions under their jurisdiction and monitor compliance with their regulations. Lastly, the Appraisal Subcommittee has primary responsibility for monitoring and reviewing the actions of the private, State, and Federal entities as they relate to Title XI.

Appraisal Foundation's Boards Establish Appraisal Standards and Minimum Appraiser Certification Criteria

The Appraisal Foundation, a nonprofit educational organization composed of groups from the real estate industry, provides the organizational framework for the ASB and AQB to carry out their Title XI-related responsibilities.[4] The ASB is responsible for setting standards for appraisals, which are contained in its Uniform Standards of Professional Appraisal Practice (USPAP). Under Title XI, these minimum standards apply to all federally related transactions for which an appraisal is required. The standards cover both the steps appraisers must take in developing appraisals and the information the appraisal report must contain.

The AQB establishes the minimum education, experience, and examination requirements for real estate appraisers that are set out in Real Property Appraiser Qualification Criteria and Interpretations of the Criteria. The AQB's criteria cover four categories of appraisers—certified general, certified residential, licensed, and trainee—each with specific education, experience, examination, and continuing education requirements. Title XI does not require States to adhere to AQB criteria for licensed appraisers or for trainees.

The ASB and the AQB regularly evaluate USPAP and the appraiser qualification criteria to determine whether revisions are needed. According to the Appraisal Foundation, both boards solicit comments from appraisers, users of appraisal services, and the public before making final changes. Since the AQB set its original criteria in 1991, for example, it has issued numerous interpretations and approved two revisions of its criteria.

State Agencies Oversee the Licensing and Certification of Real Estate Appraisers

Under Title XI, States may establish agencies to certify and license appraisers. At the time of our survey, all 50 States, the District of Columbia, and 4 of the U.S. territories had established such agencies, which typically oversee the activities of appraisers for all types of transactions, including those that are federally related. All of the States and territories had established programs for certifying appraisers,

[4] The 2002 sponsors of the Appraisal Foundation consisted of eight appraisal organizations, four affiliate organizations (representing primarily the users of appraisal services), and one international appraisal organization. In addition, over 80 organizations, corporations, and Government agencies are affiliated with the Appraisal Foundation.

and nearly 70 percent reported that they had introduced qualifications in addition to those established by the AQB.

At the time of our review, 6 States did not provide for licensed appraisers, according to the Appraisal Subcommittee. Those that did and responded to our survey reported a variety of licensing requirements. For example, some States did not require licenses unless appraisers planned to work with federally related transactions, while other States required appraisers to be either licensed or certified to perform real estate appraisals, even for transactions that are not federally related. The States' programs typically included temporary and reciprocal licensing provisions, though as discussed below, the provisions varied. (Title XI requires States to recognize on a temporary basis real estate appraisers who have been certified or licensed by another State if certain conditions are met, and encourages States to develop reciprocity agreements that readily authorize appraisers who are licensed by and in good standing with their home State to perform appraisals in other States.)

In addition to conducting certification and licensing activities, States with certifying and licensing agencies are required under Title XI to provide the Appraisal Subcommittee with the names of those appraisers who become certified or licensed in accordance with Title XI, and to collect from them an annual registry fee that goes to the Subcommittee. All of our survey respondents reported that they approve courses for appraisers' education or training, enforce State regulations concerning appraisals, and investigate complaints. Over half of the States reported that they had adopted appraisal standards in addition to those set by the ASB.

Although the States are responsible for the certification and licensing of appraisers, the Appraisal Subcommittee has a role in ensuring that State qualifications satisfy Title XI objectives. Under Title XI, the Federal financial institution regulatory agencies are to accept a State's certifications and licenses unless the Appraisal Subcommittee issues a written finding that the State certifying and licensing agency has failed to recognize and enforce the standards, requirements, and procedures of Title XI; does not have enough authority to carry out its functions under Title XI; or does not make decisions on appraisal standards and qualifications or supervise appraiser practices in a way that carries out the purposes of Title XI.

Federal Regulators Determine Which Transactions Require Appraisals and Establish Compliance Standards for Depository Institutions

Title XI requires that the Federal financial institution regulators prescribe the categories of federally related transactions that should utilize a State-certified appraiser and those that should utilize a State-licensed appraiser. The statute provides that certified appraisers must be used for federally related transactions having a value of $1,000,000 or more. The Federal financial institution regulators generally require the use of certified appraisers for commercial transactions of $250,000 or more and "complex" residential transactions of $250,000 or more. The regulators are responsible for determining whether other types of transactions warrant the use of a certified appraiser. All other federally related transactions, unless subject to an exemption as authorized under Title XI, may utilize a State-licensed appraiser.[5]

Also, under Title XI the Federal financial institution regulators may establish a threshold transaction amount at or below which neither a certified or licensed appraiser is required. As of March 15, 2004, each of the five regulatory agencies had regulations in place setting this threshold at $250,000. Thus, for federally related mortgage loan transactions of $250,000 or less, financial institutions have the option of obtaining either an appraisal or some other form of an evaluation of the property's value.[6] The regulators have issued guidelines to the institutions under their jurisdiction that specify the requirements for evaluating real estate collateral for those transactions that do not require an appraisal.

Title XI also requires the Federal financial institution regulators to ensure that real estate appraisals used in connection with federally related transactions are performed in accordance with standards developed by the ASB. The regulators require that all appraisals for federally related transactions (1) conform, at a minimum, to USPAP, (2) be written, and (3) contain sufficient information and analysis to support the institution's decision to engage in the transaction.

The Federal financial institution regulators may take informal and formal enforcement actions, including memorandums of understanding, removal, prohibition,

[5] Although the States are responsible for establishing and administering licensing qualifications, Title XI authorizes the Federal financial institution regulators to establish additional qualification criteria.

[6] For more information on real estate evaluations, see U.S. General Accounting Office, Bank and Thrift Regulation: Better Guidance Is Needed for Real Estate Evaluations, GAO/GGD–94–144,(Washington, DC: May 23, 1994). In addition, the Federal financial institution regulators issued Interagency Appraisal and Evaluation Guidelines on October 27, 1994.

and cease and desist orders and the imposition of civil money penalties, against institutions that violate their appraisal regulations. These actions can apply to contract (fee) appraisers as well as appraisers who are employees of the institutions and institution-affiliated parties. Moreover, pursuant to the FDIC Improvement Act of 1991, the Federal financial institutions regulators can take action against institution-affiliated parties such as appraisers.

Appraisal Subcommittee Monitors Title XI Regulatory Activities

Title XI created the Appraisal Subcommittee within the Federal Financial Institutions Examination Council and established it as the principal Federal agency responsible for monitoring the activities of the other components of the real estate appraisal industry oversight structure.[7] The Subcommittee has six board members—designated by the five financial institution regulatory agencies that make up the Federal Financial Institutions Examination Council, and HUD—and seven staff members. The Subcommittee funds its activities through a portion of the fees assessed by the States against individual appraisers for licensing and certification.[8]

Among other things, the Subcommittee is responsible for:

- Monitoring and reviewing the practices, procedures, activities, and organizational structure of the Appraisal Foundation, including making grants in amounts that it deems appropriate to the Appraisal Foundation to help defray costs associated with its Title XI activities. According to Subcommittee officials, the Subcommittee monitors the Appraisal Foundation by attending all significant meetings and events associated with its Title XI activities and reviewing all proposed changes or additions to its appraiser qualifications criteria or USPAP-related documents. In addition, the Subcommittee reviews the Appraisal Foundation's grant requests to ensure the requested funds will only be used for activities related to Title XI.
- Monitoring the requirements established by the States, territories, and the District of Columbia and their appraiser regulatory agencies for the certification and licensing of appraisers. Accordingly, the Subcommittee performs on-site field reviews of State agency programs and maintains communications with appraisers, State and Federal agencies, and users of appraisal services. The reviews cover open and closed complaints, approved and disapproved education providers and courses, State statutes and regulations on certifying and licensing appraisers, minutes of board meetings, appraiser registries and fees, temporary practice and reciprocity, and topical issues such as predatory lending, fraud, and illegal real estate flipping.[9] The Subcommittee issues the States letters at the conclusion of the reviews, identifying concerns, discussing whether the previous review's concerns have been resolved, and making general conclusions about the State's compliance with Title XI and Appraisal Subcommittee policy statements.

  Our analysis of the Appraisal Subcommittee's State field review letters from 1992 to 2002 found that the letters provided some information to the State regulatory agencies but lacked evidence of transparent criteria for how the Subcommittee determined and reported States' compliance levels. For example, State field review letters were sometimes inconclusive about whether the State regulatory program was in compliance. Further, when the letters contained determinations of compliance, the rationale for the decisions was not always given. For example, some States with identified concerns were deemed compliant, while others with identified concerns were deemed noncompliant. Accordingly, we recommended that the Subcommittee develop and apply consistent criteria to assess States' compliance with Title XI requirements.
- Monitoring the requirements established by the Federal financial institution regulators regarding appraisal standards for federally related transactions and determinations of which federally related transactions will require the services of State-licensed or State-certified appraisers. The Subcommittee carries out this re-

[7] The Federal Financial Institutions Examination Council is a formal interagency body empowered to prescribe uniform principles, standards, and report forms for the examination of financial institutions by the FRS, FDIC, OCC, OTS, and NCUA.

[8] Title XI authorizes the Appraisal Subcommittee to charge an annual registry fee of not more than $25. However, the Federal Financial Institutions Examination Council may approve fees up to $50 per year. As of March 15, 2004, the annual registry fee was $25.

[9] Illegal real estate flipping is a scheme where a real estate speculator buys a house, usually in a poor neighborhood, and obtains an inflated appraisal and other fraudulent financial documents to trick a lender into making a loan that exceeds the fair market value. The house is sold again at an inflated price to a second buyer. The seller has then made a large profit on the inflated value of the property. If the second buyer defaults on the loan, the mortgage lender may not be able to recoup the amount of the loan and will therefore experience a loss.

sponsibility primarily through informal channels. For example, all six Appraisal Subcommittee board members are involved in the offices responsible for appraisal regulation in their individual agencies and provide input from the Subcommittee informally to the agencies. The Subcommittee also provides technical assistance on proposed regulations on appraisal issues.

- Maintaining a national registry of State-licensed and State-certified appraisers who may perform appraisals in connection with federally related transactions.

Entities Cited Potential Impediments to Fulfilling Their Title XI Roles

The private, State, and Federal entities involved in the oversight of the real estate appraisal industry identified a number of factors that they believe could constrain their ability to fulfill their Title XI responsibilities. ASB and AQB officials stated that an impediment that they may face in the future is inadequate Federal funding, which would hinder their ability to ensure that appraisal standards and qualification criteria keep pace with changes in the mortgage industry and marketplace. State appraiser agencies reported that they often lack funding to revise their regulations with every USPAP update and to cover the increasing cost of administering the licensing and certification processes. The Federal financial institution regulators did not identify any major impediments to fulfilling their Title XI responsibilities, but noted that reaching consensus on regulatory standards was difficult because of the number of entities involved in the appraisal industry. Appraisal Subcommittee officials reported that rulemaking authority and additional enforcement sanctions could facilitate the Subcommittee's oversight of State compliance.

The Appraisal Standards and Appraiser Qualifications Board Cited Concerns about Federal Funding

ASB and AQB officials told us that expected future funding shortfalls may limit the activities they believe enhance the quality, timeliness, and usefulness of standards and qualifications. For example, the AQB chair commented that funding is needed to update their "body of knowledge," which outlines the concepts, theories, and applications of the real property appraisal profession and delineates the skill necessary to practice. According to ASB and AQB officials, the ultimate impact of funding shortfalls could be a weakening in the protections intended by Title XI because appraisal standards and appraiser qualifications may not keep pace with changes in the marketplace.

Since 1991, the Appraisal Subcommittee has allocated the Appraisal Foundation a total of over $9 million in grants to defray the costs of the two boards' Title XI-related activities. These grant allocations typically have been less than the amounts requested. For example, the ASB and AQB requested a total of over $9 million in grant money between 1994 and 2003, but less than $7 million was approved. However, the Appraisal Foundation has sources of revenue other than the Appraisal Subcommittee grants. For example, the largest source of revenue for the Appraisal Foundation in 2001 was $1.1 million from publication sales; in comparison, the $870,373 grant from the Appraisal Subcommittee represented approximately 36 percent of the Foundation's total revenue. Also, Subcommittee officials noted that the ASB and AQB had not used the entire amounts of grant funds provided in past years.

States Cited Funding Limitations and Frequent USPAP Updates as Impediments

The Appraisal Subcommittee told us that it did not have the current-year funds to fully meet the ASB's and AQB's grant requests over the past 3 years. However, the Subcommittee had a $3.9 million surplus as of December 2003. Subcommittee officials reported that the surplus built up in its early years when revenues exceeded its expenses and grants. They added that as its expenses have increased—primarily due to inflation and monitoring activity expenses—the amount of funds available for grants to the ASB and AQB from current-year funds has become limited. They further explained that it has not been Appraisal Subcommittee policy to use the surplus to provide grants to the ASB and AQB.

Appraisal Subcommittee officials also stated that they expect the boards' expenses to increase by up to 5 percent per year. Given that the number of appraisers has remained static for the last several years, Subcommittee officials did not anticipate their revenues, which are based primarily on licensing and certification fees, to increase. As a consequence, future ASB and AQB grants are expected to fall unless the Subcommittee uses its surplus, raises the $25 fee that States collect from appraisers on the Subcommittee's behalf, or both. Accordingly, we recommended that the Appraisal Subcommittee explore potential options for providing future grant funding, including drawing on its surplus if necessary, to the Appraisal Foundation and its two boards in support of their Title XI activities.

In responding to our survey, most of the States identified funding and staffing deficiencies as the most serious challenges they faced in carrying out their Title XI duties. According to Appraisal Subcommittee officials, the Subcommittee's general counsel analyzed whether the Subcommittee could provide grants to the States to help provide funding for their Title XI activities, and determined that it lacked the necessary legal authority.

Based on survey data, the average State agency had about 3 staff members, who were responsible for overseeing almost 2,000 appraisers. Many of these State agencies reported that they needed to share resources—administrative staff, office space, investigators, or all three—with other State agencies in order to perform their Title XI duties. The survey results indicated that investigations of complaints about problem appraisers suffered most from these shortages. The majority of States sharing resources were sharing investigators, who often had no real estate appraisal experience. One State official explained that without adequate funding States could not effectively administer their appraiser certification programs or investigate and dispose of disciplinary cases in a timely manner. Another State official noted that his agency knew that more enforcement and faster turnaround times in investigating complaints were needed but that limited resources hindered it. We recommended that the Appraisal Subcommittee explore potential options for funding or otherwise assisting the States in carrying out their Title XI activities, particularly the investigation of complaints against appraisers.

Seventy percent of the State appraiser regulatory agencies indicated that USPAP updates were too frequent. One State reported that frequent changes to USPAP have made processing complaints difficult because staff members have to determine what appraisal standards were in place at the time of the questionable appraisal. According to ASB officials, USPAP has been in place for only 15 years, and annual updates have been needed because so many changes have occurred in the appraisal industry. Moreover, they told us that many of the changes that have been incorporated into USPAP are a result of requests from State regulators. The officials explained that over the years the ASB has experimented with different formats for updating USPAP but has found that issuing an annual publication has been the best way to ensure that everyone is using the same standards. The ASB and the Foundation are working on developing a future publishing schedule of having USPAP issued biennially. In addition, ASB officials stated that they have recently started providing State regulators with newsletters that highlight any changes, modifications, or clarifications to USPAP or appraiser qualification criteria.

Appraisal Subcommittee Stated That Rulemaking Authority and Enforcement Options Could Facilitate Its Oversight of States

According to Subcommittee officials, the lack of rulemaking authority and limited enforcement powers make achieving the uniformity and standardization intended by Title XI more difficult. In addition, the officials noted that because the 55 State appraiser regulatory agencies took a variety of approaches to implementing Title XI, expanding the Subcommittee's role to allow it to issue regulations would help ensure greater consistency among the States in credentialing appraisers and enforcing the most current version of USPAP. However, giving the Appraisal Subcommittee rulemaking authority would also change the Subcommittee's role under Title XI from a monitoring to a regulatory function.

Subcommittee officials stated that currently the only means for ensuring State compliance with Title XI is to decertify a State. Decertification would prohibit all licensed or certified appraisers from that State from performing appraisals in conjunction with federally related transactions. Because this action is so severe and could significantly affect a State's real estate market, the Subcommittee has never used it, and its impact has not been tested. (In addition, the decertification action can be taken only for the limited purposes specified in Title XI and is subject to proof requirements and judicial review.)

The Appraisal Subcommittee noted that its oversight of the States could be strengthened if it had more enforcement authority—for example, the authority to assess monetary penalties or to require that a State stop an activity or practice. However, in commenting on a draft of our report, the Subcommittee stressed that it has always been able to ensure that States are complying with Title XI within the current supervisory and enforcement structure.

Industry Participants Raised Various Concerns about the Title XI Oversight Structure

Representatives of Federal and State regulatory agencies, appraiser trade groups and education providers, and the mortgage industry expressed various concerns and

conflicting viewpoints about the Title XI regulatory structure. However, there was no clear consensus regarding the need for or impact of possible changes.

Differences Among State Licensing Programs

According to many of the groups we contacted, Title XI's most significant shortcoming is the provision that leaves the criteria for licensed appraisers to each State, including decisions such as how often appraisers should be licensed and whether they should be licensed at all. According to an official from the Appraisal Subcommittee, Title XI's intent was to ensure that appraisers for federally related transactions met minimum requirements for experience and education and had been examined in order to ensure a minimum level of competency. But Title XI specifically provides that the Appraisal Subcommittee will not set requirements for licensing and that any Subcommittee recommendations are nonbinding. Some groups believe that this provision has led to a lack of uniform qualifications in licensing across the country (for example, in education and experience) and may also have helped to create an environment conducive to mortgage fraud.

At the time of our review, officials from the Appraisal Subcommittee reported that most States have adopted provisions requiring that licensed appraisers meet AQB recommended criteria. However, six States did not have a State-licensed appraiser category, and six had licensing requirements that were less stringent than the AQB's. As a result, Subcommittee officials said, some licensed appraisers may not meet recommended qualifications criteria. For example, in 2002, one State passed legislation that eliminated the experience requirement for its licensed appraisers; and, in 2001, another State revised its licensing criteria to comply with AQB requirements but at the same time "grandfathered" in several hundred licensed appraisers.

According to two regulatory officials, problems related to the lack of uniformity in licensing appraisers are compounded by the fact that Title XI also makes licensing voluntary at the State level. Voluntary licensing means that the State does not have a legislative requirement that appraisers be licensed or certified. However, the volunteer States do provide the opportunity for an appraiser to become licensed or certified in order to perform federally related transactions. As of March 2003, 10 States were classified as being in the voluntary licensing category. Some regulators, as well as one appraiser trade group, view voluntary licensing as a serious flaw in the industry's regulatory structure and a probable contributor to mortgage fraud. Moreover, voluntary licensing may indirectly place the onus on financial institutions to ensure that appraisers for federally related transactions have the appropriate qualifications. One Federal financial institution regulator reported that most of the mortgage fraud problems it has encountered have occurred in States where licensing is voluntary. An earlier Federal Bureau of Investigation testimony at a special Congressional hearing on predatory lending in March 2000 echoed this view. According to that testimony, the most egregious property flipping problems have occurred in States where licensing is voluntary for transactions that are not federally related.

Industry participants also cited a lack of uniformity in the way States grant temporary and reciprocal licenses. Because a State may not recognize the credentials from another State, appraisers often have to carry multiple State licenses. The Appraisal Subcommittee has issued policy statements on temporary practice and encouraging reciprocity. However, our survey indicated that State regulatory agencies continue to vary widely on these issues. For example, of the 53 States and territories that responded to this question, 40 issued temporary licenses for single assignments, 16 allowed an appraiser only one temporary license at a time, and 15 limited the number of temporary licenses an appraiser could receive annually. Six of the 54 respondents to our survey indicated that visiting appraisers are required to pass a State exam in order to receive a reciprocal license. This practice is inconsistent with the Appraisal Subcommittee's guidance recommending that States accept licenses or certification from other States meeting AQB requirements.

Transactions Not Covered by Title XI

Industry participants also voiced concerns about the fact that Title XI does not cover all financial institutions and that mortgage brokers are not subject to Federal regulation. When Title XI was enacted, federally regulated lending institutions (banks, thrifts, and credit unions) made most mortgage loans. Today, other financial institutions, such as mortgage bankers and finance companies, account for a substantial share of the mortgage marketplace. Many of these financial institutions that are not federally regulated, as well as an increasing portion of regulated financial institutions, use mortgage brokers to originate loans, so that these brokers now originate about 50 percent of all mortgage loans. These entities and individuals may have State licenses, but they are not monitored by Federal or State entities through,

for example, examinations or audits.[10] Appraisers have anecdotally reported that these originators pressure them the most to appraise properties at or near the purchase price to assure that the mortgage transaction will occur.

Some industry participants have said that the $250,000 real estate appraisal threshold established by the Federal financial institution regulators undercuts efforts to protect consumers. These groups believe that oversight of real estate appraisals should be geared toward the interests of consumers, who should be able to expect an unbiased, objective third-party opinion of the value of real property offered as security for a loan. However, Title XI was enacted in response to the impact of appraisal problems on federally insured depository institutions, and Federal financial institution regulators have identified few problems or risks to depository institutions associated with loans valued below the $250,000 threshold.

Costs and Lack of Uniform Approval Processes for Appraiser Education Courses

Several State regulators and education providers expressed concerns about the expenses and lack of uniformity in the processes associated with approving instructors and courses for appraisers' continuing education. A representative of an appraisers' trade group noted that gaining approval for a course and an instructor in one State does not necessarily translate into approval in other States. As a result, the trade group spent around $30,000 having courses for a July 2000 training conference approved in all jurisdictions. Some appraisal industry participants believe that the added cost and procedures involved in acquiring approval in each State is overly burdensome.

AQB officials told us that the board has set up a voluntary national system for approving courses and that these concerns had influenced their project. According to the AQB, the course approval program was designed to be a convenience for both course providers and State regulators while helping to ensure quality appraisal courses. However, AQB's course and instructor approval programs have met opposition in some quarters. For example, some State officials and other industry participants stated that requiring AQB approval for all USPAP refresher courses and instructors and restricting course materials and examinations to AQB publications—for which AQB charges a royalty fee—represent a conflict of interest. In addition, some education providers have stated that the fees charged by the AQB for its course and instructor approval are excessive. On the other hand, some State and Federal financial institution regulators believe that the Appraisal Foundation and its boards possess expertise and resources the States do not have and thus are needed to ensure that the quality of appraiser education and training is not compromised.

Similarly, some States and educators have expressed concern that the AQB and Appraisal Subcommittee have encroached upon State authority in setting certain appraisal standards and appraiser qualifications. For example, the regulatory agency and an education provider in one State objected to certain AQB education requirements for certified appraisers, in particular a requirement that education providers be certified through the AQB's instructor certification program. As part of its industry monitoring function, the Appraisal Subcommittee reviewed those standards and determined that the AQB had acted appropriately in adopting them. The Appraisal Subcommittee also requested a legal opinion from the Legal Advisory Group of the Federal Financial Institutions Examination Council on the scope of AQB's authority to adopt education-related standards for certified appraisers; the scope of the Appraisal Subcommittee's responsibility in monitoring the AQB; and the Appraisal Subcommittee's authority to oversee State regulators' implementation of AQB standards.[11] In a June 2002 opinion, the Legal Advisory Group concluded that the AQB's and Appraisal Subcommittee's actions appeared to be consistent with and authorized by Title XI.

Variations in State Regulatory Agencies' Enforcement of Title XI Requirements

Some industry participants reported a lack of uniformity in processing complaints and taking disciplinary actions against those problem appraisers that were referred to State regulatory authorities. We analyzed data States submitted to the Appraisal Subcommittee and found that the number of disciplinary actions taken differed widely. For example, one State reported taking only a single disciplinary action,

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[10] Fannie Mae officials noted that when an appraisal is required for a mortgage that will be delivered for sale to the GSE, mortgage brokers must use appraisers that are State-licensed or certified in accordance with Title XI.

[11] The Legal Advisory Group consists of the general or chief counsels of the FDIC, FRS, OCC, OTS, and NCUA.

while two other States accounted for over 25 percent of the 4,360 disciplinary actions reported as of October 31, 2002.

Several entities reported that States' complaint filing requirements ranged from simple to onerous. For example, some States require simply that complainants submit information on an allegation, while others accept complaints only on a specific form, or require that complaint documents be notarized or that complainants provide witnesses and testify against appraisers. Other concerns included:

- The length of time needed to resolve complaints. For example, one State required 1 to 2 years, potentially allowing the appraiser to continue what might be fraudulent or questionable practices.
- Statutes of limitations that pose an obstacle in penalizing appraisal violators. For example, statutes in at least three States prohibit both investigations into and punitive actions for unlawful appraisal activities that allegedly took place more than 3 to 5 years earlier.

In addition to concerns about the complaint process, industry participants reported misgivings about outcomes, including disciplinary actions and feedback. For example, Fannie Mae officials commented that they had been dissatisfied with some State decisions on punitive actions and with the lack of feedback on actions that had actually been taken. The officials added that some States do not penalize appraisers for multiple violations if the appraisers have already been disciplined or do not tell complainants what action was taken. As an example, they noted that some States appeared to perform meaningful investigations and took appropriate actions while others appeared unwilling to investigate similar cases with comparable support and documentation. HUD officials echoed this view, saying that States typically do not take action when they are notified that an enforcement action has been taken against an appraiser. Another industry participant reported that there is little incentive to make referrals given the fact that there is no assurance that the State will take action.

According to Appraisal Subcommittee officials, a number of States have told them that the referral information that Fannie Mae and HUD have provided to the States is frequently in a format or manner that they cannot readily absorb or use. For example, some of the States indicated that they received over a hundred referrals from Fannie Mae as one group, which overwhelmed the States' ability to review and investigate the referrals in a timely basis. Other States stated that the referrals were for real estate transactions for which the State's statute of limitations had already expired. To improve the process for referring problem appraisals by entities that oversee or use real estate appraisals to the State appraiser agencies for possible enforcement actions, we recommended that the Appraisal Subcommittee work with Fannie Mae, Freddie Mac, and HUD to ensure that the referral of problem appraisals (1) are provided in a format that is useful to the State appraiser agencies and (2) facilitate the Subcommittee's efforts to monitor decisions made by the States regarding the supervision of appraiser practices.

No Clear Consensus Regarding the Need for Changes to the Title XI Regulatory Structure

Among the various representatives of trade groups, education providers, and other industry participants that we contacted, there were differing opinions as to what, if any, changes were necessary to Title XI. Likewise, the responses to the survey that we sent to the State appraiser agencies did not indicate a clear consensus regarding States' views of the impacts of eliminating some of the central aspects of the Title XI regulatory structure. Some officials from State appraiser agencies have expressed strong viewpoints regarding the need for changes to Title XI. For example, an official from one of the State appraiser regulatory agencies stated that the States are now in a position to oversee the real estate appraisal industry without any Federal involvement, much as they do other professions. He suggested that Congress eliminate the Appraisal Foundation and the AQB and make the ASB independent and self-supporting. An official from another State regulatory agency said that to correct the present system's problems, Congress would need to completely restructure the Title XI structure. He recommended eliminating the Appraisal Subcommittee and the Appraisal Foundation, replacing them with a new board at the Federal level. The new board would represent the appraisal industry more broadly and have strong Congressional accountability. He also suggested that Congress clearly designate the States as having sole responsibility for administering and enforcing Title XI.

However, our survey of the State appraisal agencies showed a wide variety of views. For example, 22 States and territories (41 percent) said that eliminating the Appraisal Subcommittee would enhance their ability to regulate appraisers, while

17 (31 percent) responded that eliminating the Subcommittee would be a hindrance. The remaining States felt that not having the Subcommittee would neither help nor hinder regulation. Similarly, 31 and 23 States, respectively, indicated that eliminating the ASB and AQB would hinder their efforts to regulate appraisers, while 10 and 21 States, respectively, indicated that eliminating the ASB and AQB would be helpful.

In conclusion, Title XI brought about significant changes in the real estate appraisal industry. According to Federal financial institution regulators, real estate appraisals have not been a major factor in the failure of federally insured financial institutions since the passage of Title XI. However, opportunities exist to enhance the effectiveness of the current regulatory system to help ensure that federally related transactions are based on accurate assessments of the value of properties used as collateral for loans.

Mr. Chairman, this concludes my prepared statement. I would be happy to answer any questions at this time.

PREPARED STATEMENT OF STEVEN D. FRITTS

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FEDERAL FINANCIAL INSTITUTION EXAMINATION COUNCIL
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FEDERAL DEPOSIT INSURANCE CORPORATION

MARCH 24, 2004

Introduction and Background

Good afternoon, Chairman Allard and Members of the Subcommittee. Thank you for the opportunity to discuss the current state of the appraisal industry and its Federal and State oversight. On behalf of the Appraisal Subcommittee (ASC), I commend your Subcommittee's initiative to understand the current state of the industry and assess the current regulatory structure and its ability to ensure that Federal financial and public policy interests in real estate related financial transactions are protected, consistent with Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, as amended (Title XI).

I am the Chairman of the Appraisal Subcommittee. The Chairmanship of the Appraisal Subcommittee, which was created on August 9, 1989, pursuant to Title XI, rotates bi-annually among the Subcommittee membership. I also serve as Associate Director at the FDIC, where my responsibilities involve safety and soundness of bank examination policy.

In general, the ASC oversees the real estate appraisal process as it relates to Federally related transactions—any real estate related financial transaction entered into on or after August 9, 1990, that a Federal banking agency or any regulated depository institution engages in or contracts for, and requires the services of an appraiser. The ASC membership includes representatives from each of the five members of the Federal Financial Institutions Examination Council, and from the Department of Housing and Urban Development.

Following the financial crisis of the 1980's, Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Title XI of FIRREA addressed the identified weaknesses regarding real property appraisals used in connection with federally related transactions. Prior to FIRREA, appraisals for federally related transactions and the appraisers who performed them, were, for the most part, unregulated at either the Federal or State level. In most States, the only legal requirement to become an appraiser was that the individual obtain a business license from the county or other local jurisdiction. During the financial crisis of the 1980's, poor quality appraisals were a contributing factor to the numerous bank and savings and loan failures. Title XI sought to address this situation.

Title XI created a unique system. As noted in the General Accounting Office (GAO) May 2003 report titled, *Opportunities to Enhance Oversight of the Real Estate Appraisal Industry,* Title XI created a complex oversight structure for real estate appraisals and appraisers that involves private, State, and Federal entities. Two private entities within the Appraisal Foundation establish uniform rules for real estate appraisals (that is, the Uniform Standards of Professional Appraisal Practice (USPAP)) and set minimum criteria for certifying appraisers (that is, The Real Property Appraiser Qualification Criteria). The Appraisal Standards Board and the Appraiser Qualifications Board, respectively, establish these rules and criteria.

State regulatory agencies (that is, 50 States, the District of Columbia, and five territories) certify appraisers based on these criteria. The Federal financial regulatory agencies (Agencies) oversee financial institutions' use of appraisals.

Responsibilities of the Appraisal Subcommittee

Title XI sets out the ASC's general responsibilities:

- Monitor the requirements established by the States, territories, and the District of Columbia and their appraiser regulatory agencies (State agencies) for the certification and licensing of appraisers. The ASC reviews each State's compliance with the requirements of Title XI and is authorized by Title XI to take action against noncomplying States;
- Monitor the requirements established by the agencies regarding appraisal standards for federally related transactions and determinations of which federally related transactions will require the services of State-licensed or State-certified appraisers;
- Maintain a national registry of State-licensed and certified appraisers who may perform appraisals in connection with federally related transactions;
- Monitor and review the practices, procedures, activities, and organizational structure of the Appraisal Foundation; and
- Transmit an annual report to Congress regarding the activities of the ASC during the preceding year.

The ASC is funded by a $25 per year fee for an appraiser to be listed on the National Registry of State-Certified and Licensed Appraisers (Registry). States collect these fees as part of their licensing, certification, and renewal activities and remit the registry fees to the ASC. Although the ASC has the authority to increase the fee up to $50, we have maintained the registry fee at the same $25 that was established in 1989. The annual operating budget of the ASC is $2.1 million. Through automation and contracting out, the ASC has reduced staffing from nine employees to 7 over the last 15 years and has attempted to maintain a high level of operating efficiency.

Status of State Compliance with Title XI

Generally, States do a good overall job of enforcing compliance with Title XI, given the resource limitations facing most States. Although some States have areas that need improvement, we have found most States generally compliant with Title XI.

Our primary tool for evaluating State compliance with Title XI is a 3-year on-site review cycle. Given Title XI's 56 jurisdictions, ASC staff performs on-site reviews of approximately 18 States per year, plus conducting several follow-up reviews. Once we have completed the field review and formally transmitted our findings to the State, we work with the State to ensure correction of noted areas of concern. Most States address our concerns in a timely manner. Currently, the most problematic area involves complaint investigation and resolution. Because this area requires specialized personnel and expertise, it is one of the more complex and costly functions for State appraiser regulatory agencies. Consequently, some States are not as timely in their complaint investigation and resolution efforts as they should be. Each year, we provide a summary of significant areas of concern identified during our field reviews in our annual report to Congress.

National Registry of State-Certified and Licensed Appraisers

One of the ASC's primary responsibilities is maintenance of the registry. During the past several years, the ASC has made the registry available via the Internet to States and the public. We added sections reserved for State-only access to facilitate State efforts in areas such as researching the license history of appraisers and determining whether an appraiser is in "good standing" in another State. We have added automated e-mail notification to States, lenders, and other parties when appraiser credentials are revoked or suspended and when they expire. We continue to evaluate the registry to add features that improve its value to the States, lenders, and the general public.

Appraisal Foundation

The ASC monitors the activities of the Appraisal Foundation and its Appraiser Qualifications Board and Appraisal Standards Board to ensure that their actions are reasonable, not arbitrary or capricious, and otherwise consistent with law. As authorized by Title XI, the ASC also provides funding, via annual grants, to the Foundation and its boards to support their Title XI-related activities.

Challenges Ahead for the Appraiser Industry

In many cases, it is difficult for appraisers licensed or certified in one State to appraise properties in other States. Title XI requires that States issue temporary practice permits to appraisers on a single assignment basis, but imposes this requirement only for federally related transactions. Also, the appraiser must apply each time he or she wishes to perform an assignment in that State. Often, delays in completing the temporary practice approval process conflict with the timing needs of the parties involved in the real estate transactions.

While Title XI requires States to offer temporary practice for federally related transactions, it only encourages States to offer license and certification credentials via reciprocity agreements with other States. To enter into such agreements, some States require formal written agreements with other States, while other States' laws prohibit them from entering into such formal agreements. Some States have developed methods of informally offering reciprocity to appraisers. Nonetheless, impediments to interstate movement of appraisers are a concern repeatedly expressed to us by lenders and appraisers with regional or national operations.

With 56 Title XI jurisdictions issuing implementing statutes and regulations, there is a considerable amount of conflict and overlap among the States. For example, appraisers who hold appraiser credentials in multiple States might have to take the same continuing education course multiple times to meet the continuing education requirements of various States. Additionally, a continuing education course that is acceptable to one State might not be acceptable to another.

Another issue, which was raised in the GAO report, is the applicability of Title XI to residential mortgage transactions handled by mortgage brokers. These entities were not captured by Title XI as most mortgage brokers are not regulated at the Federal or State level. The ASC raises this issue as we have received a number of comments on appraisal abuse by mortgage brokers. Many estimates indicate that mortgage brokers originate as much as 50 percent of all residential mortgage loans.

Other issues that the industry and regulators are grappling with include the appropriateness of automated evaluation methodologies and the rapidly increasing market values of residential properties in some markets.

Conclusion

Some contend that the need for Federal law and Federal oversight of the appraiser regulatory system no longer exists. Given the difficulties we have experienced in achieving some level of consistency among States to better facilitate interstate lending and appraising activities, we believe that a lack of Federal law and oversight would allow the system to become increasingly fragmented to the overall detriment of the appraisal industry.

Considering the complexity inherent in the appraiser regulatory structure and the weaknesses discussed above, the system functions reasonably well. At 15 years, the appraiser regulatory system is relatively young. We expect continued adjustments and challenges as the system matures.

This concludes my testimony. I will be happy to answer any questions the Subcommittee might have.

PREPARED STATEMENT OF DAVID S. BUNTON

EXECUTIVE VICE PRESIDENT, THE APPRAISAL FOUNDATION

MARCH 24, 2004

Introduction

Mr. Chairman, The Appraisal Foundation appreciates the opportunity to appear before the Subcommittee on Housing and Transportation of the Senate Committee on Banking, Housing, and Urban Affairs and offer its perspective on Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA), 15 years after enactment.

Background

My name is David Bunton and I serve as the Executive Vice President of The Appraisal Foundation. Our organization plays a somewhat unique role in that it serves as the private sector resource to appraiser regulators. We are not a membership-based trade association, but rather a not-for-profit educational organization that serves as an umbrella group for organizations with an interest in valuation. We refer to these groups as Sponsoring Organizations, a listing of which is attached to this testimony as Attachment #1.

The appraisal profession in the United States has traditionally been somewhat fragmented. In the interest of promoting consistency and uniformity in the areas of professional standards and qualifications, eight national appraisal organizations created The Appraisal Foundation in 1987. Our mission is to promote professionalism in appraising by setting qualifications that one must meet to *become an appraiser* and establishing performance standards for *how an appraisal should be performed.*

Our Congressionally Authorized Responsibilities

In 1989, through the enactment of Title XI of FIRREA, the Congress gave The Appraisal Foundation specific responsibilities relating to the regulation of appraisers. All appraisals performed for federally related transactions must be in conformance with generally accepted appraisal standards, which are known as the *Uniform Standards of Professional Appraisal Practice* (USPAP) and are promulgated by the Appraisal Standards Board of The Appraisal Foundation. It is these standards which are used by the State appraiser regulatory agencies for disciplinary purposes.

In addition, Title XI mandates that State-certified real estate appraisers must meet the minimum qualifications established by the Appraiser Qualifications Board of The Appraisal Foundation. These qualifications include education, experience, and continuing education requirements.

Finally, in order to become a State-certified real estate appraiser, an individual must achieve a passing grade on a State certification examination that has been reviewed and approved by the Appraiser Qualifications Board.

A Unique System for a Unique Task

There is no question that Title XI established a rather unique relationship between Federal regulators, State regulators, and the private sector. However, given the unique task at hand, it is working quite well.

The Appraisal Foundation establishes the minimum qualification and performance thresholds that ensure a base level of competency. The 55 States and territories regulating appraisers then use these thresholds and, if they so choose can raise them to facilitate the specific needs of their jurisdiction. The Federal oversight entity, the Appraisal Subcommittee, ensures each of the 55 jurisdictions is operating in a manner that is consistent with Congressional intent. The Appraisal Subcommittee also monitors the activities of The Appraisal Foundation to ensure that it is fulfilling its Title XI responsibilities. This hybrid system (a) ensures that minimum levels of competency are met, (b) provides administrative latitude to each of the States, and (c) ensures overall accountability.

In addition, this regulatory system does not operate with annual Congressional appropriations. Rather it is funded by appraisers through an annual "registry fee," currently $25.00, which is paid to the Appraisal Subcommittee. This fee offsets the operating expenses of the Appraisal Subcommittee, as well as a significant portion of the expenses of the Appraisal Standards Board and the Appraiser Qualifications Board.

One of the ancillary benefits of this system is that over the past decade a very productive working relationship has developed between the three entities. Foundation representatives participate in all State regulator conferences and we have conducted training sessions specifically for State appraiser investigators. We also have frequent meetings with Appraisal Subcommittee representatives. From our perspective, the input we have received from the States and the Appraisal Subcommittee has been invaluable in ensuring that the work of our Boards continues to meet the needs of the regulatory community and the marketplace.

What Has Been Accomplished

Over the past 15 years, The Appraisal Foundation has taken its Congressionally authorized responsibilities very seriously. As I previously indicated, our work has focused on two areas: Appraiser qualifications and standards of professional practice.

Appraiser Qualifications

During the implementation period of Title XI, the lending community expressed strong concerns that, if the qualifications for appraisers were set too high, there would be a subsequent shortage of appraisers which would impede lending. This concern was coupled with the fact that there was very little, if any, demographic information available about appraisers.

With this in mind, the Appraiser Qualifications Board initially set relatively modest thresholds for education, experience, and examination requirements to become a State-certified real estate appraiser. The philosophy of the Board then, as it is now, was to periodically increase the qualifications over time to ensure continued appraiser competency and reflect changes in technology and the needs of the mar-

ketplace. Subsequent increases in appraiser qualifications became effective in 1998 and 2003, with another increase scheduled for implementation in 2008.

For some time, Federal and State regulators had shared their concerns with The Appraisal Foundation about deficiencies in USPAP education (the quality of the course materials as well as the competency of the instructors). Very few would argue that sound education is an essential component of understanding USPAP due to the complexities of the document and its evolving nature.

In response to this problem, in 2000 the Appraiser Qualifications Board (AQB) adopted new criteria intended to improve the overall quality of USPAP education. The changes, which became effective on January 1, 2003, include:

- Consistent Course Content: USPAP courses taken for qualifying and continuing education must be the *National USPAP Courses* or their equivalent. For 2004, 11 courses developed by educational providers have been deemed to be equivalent to the *National USPAP Courses.*
- Instructor Competency: In order for an appraiser to receive State credit for attending a USPAP course, it must have been taught by an AQB Certified USPAP Instructor and State-certified appraiser. In order to become an AQB Certified USPAP Instructor, an individual must attend a 2-day course and receive a passing grade on a comprehensive examination. As of this date, 462 individuals have become AQB Certified USPAP Instructors.
- Increased USPAP Continuing Education Requirement: Continuing education requirements for real property appraisers were modified to require 7 hours of USPAP instruction every 2 years. There was previously no specific requirement for USPAP continuing education.

The Appraiser Qualifications Board is also responsible for the content of the examinations used by the States to certify appraisers. With the assistance of an outside psychometric consultant, the Board has developed and updated examination content outlines for use in the review and approval of State examinations. The AQB conducted comprehensive reviews of the State appraiser examinations in 1991, 1995, and 2002.

Standards of Professional Practice

Since the enactment of Title XI, the distribution of the generally accepted appraisal standards, USPAP, has received wide dissemination, increasing from 10,000 copies annually in the early 1990's to 80,000 copies in 2003. With this increased exposure has come a considerable increase in the number of inquiries to the authors of USPAP, the Appraisal Standards Board. Accordingly, the Appraisal Standards Board has offered a significant amount of guidance to appraisers on performing appraisals in conformance with these standards.

The Board conducts public meetings around the Nation and publicly exposes all proposed changes to USPAP. Any changes to USPAP must be adopted in a public meeting. The Board has issued 27 Advisory Opinions to date and publishes Questions and Answers on USPAP every month on the Foundation website (*www.appraisalfoundation.org*). The USPAP document is available to the general public on the Foundation website and all appraiser regulators are granted permission to reproduce the document free of charge.

At the time of enactment of Title XI, USPAP was revised periodically throughout the year (as often as quarterly). The standards were subsequently published in a format that was revised twice a year and for the past several years have been published on an annual basis. It is our hope to publish USPAP once every 2 years in the near future. In order to promote consistent USPAP enforcement among the States, the Foundation has published two editions of a publication entitled *A Digest of Court Cases and Administrative Rulings Citing USPAP.*

Advisory Councils

In order to ensure that the work product of our two Boards continues to reflect the needs of the regulatory community and the marketplace, we have established two advisory councils. One council, known as The Appraisal Foundation Advisory Council, has over fifty members that are either nonprofit organizations or Government agencies. The membership of this diverse group ranges from the American Bankers Association and the National Association of Realtors to the U.S. Department of Justice and the Internal Revenue Service.

Our other advisory council, the Industry Advisory Council, provides valuable input from the for-profit sector. Members of this council include such companies as the Bank of America, Deloitte & Touche, Washington Mutual, Prudential Insurance, and Wells Fargo. Membership listings of both advisory councils are included with this testimony as Attachments #2 and #3.

Government Assignments Beyond Title XI

In recent years, The Appraisal Foundation has also provided assistance to the Federal Government outside of its specific Title XI responsibilities. Because we are viewed as an objective, unbiased resource, we have been approached by several Federal Government agencies to perform evaluations on their behalf. We have been engaged by the U.S. Forest Service, the Bureau of Land Management, the Inspector General of the Department of Interior, and the Office of Special Trustee for American Indians to perform evaluations of their appraisal policies and procedures.

Title XI Is Working as Intended

One of the most tangible measurements of how Title XI has performed is a review of the disciplinary action taken by the States for the period of 1992–2002. During that time period, a total of 4,360 disciplinary actions were reported by the States to the Appraisal Subcommittee. Of these, over 1,250 were serious violations which resulted in the suspension, revocation, or voluntary surrendering of an appraiser's State credential; over 1,200 individuals that, due to competency or conduct, were no longer permitted to make value determinations in federally related transactions.

As to alternatives to the existing structure of Title XI, it is important to keep several factors in mind. First, the Federal Registry of real estate appraisers maintained by the Appraisal Subcommittee currently contains over 95,000 appraisers. Accounting for individuals who hold a credential in more than one State, the total number of real estate appraisers is estimated to be approximately 80,000. There are several fine national appraisal organizations, including the Appraisal Institute and the American Society of Appraisers in attendance today. However, the majority of real estate appraisers in the United States are not affiliated with any professional appraisal organization. Accordingly, absent the current system, any type of "self-regulating" alternative is virtually impossible due to the fact that most appraisers are not subject to peer review procedures.

Regarding the elimination or dilution of the Federal oversight component of Title XI, it is important to remember that Title XI was enacted, not as consumer protection legislation, but rather from a safety and soundness perspective to ensure the integrity of the deposit insurance fund. That need continues to exist today and should not be delegated exclusively to the 55 States and territories regulating appraisers.

For example, the States currently adhere to the minimum standards and qualification thresholds established by The Appraisal Foundation because they are required to by law. Absent that requirement, States would be free to establish very low threshold levels or none at all. This could severely impact the competency of appraisers and meaningful enforcement in certain States and have a significant negative effect on consistency among all of the States. Without credible enforcement, there could be a detrimental impact on the safety and soundness of the nation's lending institutions.

Recommendations

As stated above, we believe that Title XI is generally working as intended and should remain intact. However, in the event that specific improvements were sought, The Appraisal Foundation would offer the following recommendations:

- *Greater Regulatory Latitude for the Appraisal Subcommittee:* The Appraisal Subcommittee should be given a series of graduated regulatory options for oversight of the State appraiser regulatory programs; as opposed to the single option it now is provided.
- *State-Licensed Appraisers Should Meet the Qualification and Examination Requirements of the Appraiser Qualifications Board:* The State licensure category was a last minute addition to Title XI. It appears that not including the State *licensed* classification along with the State *certified* classifications was an oversight.
- *Mandate Reciprocity Among the States:* With the ongoing consolidation of the lending community, it is in the interest of improved interstate commerce that artificial barriers to practice be removed. At present, the Appraisal Subcommittee is charged with only "encouraging" reciprocity.

Conclusion

Mr. Chairman, when recently confronted with concerns about the accounting profession relating to Enron, Worldcom, and Arthur Andersen, the Senate Banking Committee addressed the issue by increasing Federal oversight through the creation of the Public Company Accounting Oversight Board (PCAOB). Similarly, with the revelations about financial reporting variances at Freddie Mac, this Committee is

pursuing options for greater Federal oversight of the Government Sponsored Enterprises (GSE's).

Fifteen years ago, your colleagues were faced with a deposit insurance crisis and opted to create a regulatory system that includes Federal oversight of the State regulatory programs that credential the individuals who determine the value of the underlying assets of our financial institutions. To dilute or remove Federal oversight at this time would be sending the wrong message at the wrong time.

Again, we appreciate the opportunity to share our perspective with you today and would be pleased to answer any questions.

Attachment #1

Sponsoring Organizations of The Appraisal Foundation

Appraisal Sponsors

American Society of Appraisers

American Society of Farm Managers & Rural Appraisers

Appraisal Institute

International Right of Way Association

International Association of Assessing Officers

Massachusetts Board of Real Estate Appraisers

National Association of Independent Fee Appraisers

National Association of Master Appraisers

Affiliate Sponsors

American Bankers Association

Farm Credit Council

Mortgage Insurance Companies of America

National Association of Realtors

Attachment #2

The Appraisal Foundation Advisory Council

2004 Members

American Bankers Association
American Institute of Certified Public Accountants
American Society of Appraisers
American Society of Farm Managers and Rural Appraisers
America's Community Bankers
Appraisal Institute
Appraisers Association of America
Association of Appraiser Regulatory Officials
Association of Machinery & Equipment Appraisers
California Association of Real Estate Appraisers
Canadian National Association of Real Estate Appraisers
Columbia Society of Real Estate Appraisers
Conference of State Bank Supervisors
Counselors of Real Estate
Employee Relocation Council
Equipment Appraisers Association of North America
Fannie Mae
Farm Credit Council
Federal Agricultural Mortgage Corporation
Federal Deposit Insurance Corporation
Federal Highway Administration
Freddie Mac
General Service Administration
Institute for Professionals in Taxation
Internal Revenue Service
International Association of Assessing Officers
International Right of Way Association
International Society of Appraisers
Manufactured Housing Institute

Maryland Association of Appraisers
Massachusetts Board of Real Estate Appraisers
Mid-West Appraisers Association
Mortgage Bankers Association of America
Mortgage Insurance Companies of America
National Association of Environmental Risk Auditors
National Association of Federal Credit Unions
National Association of Home Builders
National Association of Independent Fee Appraisers
National Association of Master Appraisers
National Association of Mortgage Brokers
National Association of Real Estate Brokers
National Association of Realtors
National Auctioneers Association
National Council of Real Estate Investment Fiduciaries
National Society of Real Estate Appraisers
Office of Thrift Supervision
US Department of Agriculture, Farm Service Agency
US Department of Agriculture, Forest Service
US Department of the Army
US Department of Housing and Urban Development
US Department of the Interior Bureau of Land Management
US Department of the Interior Fish & Wildlife Service
US Department of the Interior National Park Service
US Department of Justice
US Department of the Navy
US Department of Veteran Affairs
US Environmental Protection Agency

Participating Observers
Appraisal Subcommittee
TAFAC's Board of Trustees Representatives

Attachment #3

Industry Advisory Council

2004 Members

American Appraisal Associates, Inc.
America's Cutting Edge Real Estate Services
Appraisal Forum
Appraisal.com
ATM Corporation of America
Bank of America
Bank One Corporation
C&S Marketing
CB Richard Ellis
Chesapeake Appraisal & Settlement Services Inc./ Citigroup
Cushman & Wakefield, Inc.
Deloitte & Touche
eAppraiseIT LLC.
EquiFirst
FNC, INC.
General American Corporation
Houlihan, Lokey, Howard, & Zukin
Kennedy Associates Real Estate Counsel, Inc
Landsafe
Lehman Brothers / Aurora Loan Services
Liability Insurance Administrators
Marshall & Stevens, Inc.
Mortgage Information Services, Inc
Option One Mortgage
Price Waterhouse Coopers
Prudential Financial
Valuation Information Technology, Inc.
Wachovia Bank
Washington Mutual Bank
Wells Fargo Bank
Willamette Management Associates, Inc.

PREPARED STATEMENT OF ALAN EUGENE HUMMEL, SRA

IMMEDIATE PAST PRESIDENT, THE APPRAISAL INSTITUTE
CHIEF EXECUTIVE OFFICER, IOWA RESIDENTIAL APPRAISAL COMPANY
ON BEHALF OF
THE APPRAISAL INSTITUTE AND
THE AMERICAN SOCIETY OF FARM MANAGERS AND RURAL APPRAISERS

MARCH 24, 2004

Chairman Allard and Members of the Subcommittee, I am Alan Eugene Hummel, President of Iowa Residential Appraisal Company in Des Moines, Iowa, and Immediate Past President of the Appraisal Institute. I am pleased to be here today on behalf of the Appraisal Institute and the American Society of Farm Managers and Rural Appraisers, which together represent more than 20,000 real estate appraisers in the United States. Thank you for holding this hearing on the effectiveness of Federal requirements established approximately 15 years ago that marked the beginning of Federal involvement in State-licensing and certification requirements for real estate appraisers in the United States.

Real estate appraisers play a strategic role in our country's real estate financing system. A professional appraiser's objectivity, training, experience, and ethics are fundamental characteristics that help participants in residential and commercial real estate mortgage transactions assess the value of real estate and understand the risks involved in collateral lending. Trillions of dollars are invested in real estate in the United States, so it is of paramount importance that appraisers be qualified and adequately trained and have sufficient experience in the type of property under consideration. Also important is a system of enforcement with the authority to help ensure that appraisers are properly educated and experienced.

Both the appraisal profession in general and our professional organizations in particular have been directly impacted by the implementation of Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). We have serious concerns with how the law and subsequent regulation is affecting the profession. We are concerned with the quality of appraisals being used in our Nation's mortgage financing system today. A fundamental goal of FIRREA was to raise the professionalism of appraisers involved in federally related real estate transactions; yet we have concluded that this goal has not been met. In fact, the result has been to promote a system that lessens the professionalism of appraisers rather than strengthens it. Having provided for only "minimum" qualification requirements and meager oversight authority, the implementation of FIRREA has failed to offer incentives to appraisers to seek additional training, education, and experience. In addition, many State appraiser licensing boards and the Federal oversight authority allow bad actors to remain in the system.

Competent and qualified real estate appraisers serve as a crucial safeguard in our banking system, but lax enforcement and ineffective Federal oversight serve to diminish this safeguard. Thus, we are here to alert Congress that the system FIRREA envisioned is broken and needs to be fixed if we are to avoid a financial crisis on the scale of the Savings and Loan disaster of the 1980's or the accounting scandals in the 1990's.

Appraiser Regulatory Structure

As you know, the Savings and Loan crisis of the 1980's led Congress to enact FIRREA. Title XI, the "Real Estate Appraisal Reform Amendments," was enacted to protect Federal financial and public policy interests in real estate related transactions by requiring that real estate appraisals be performed by individuals with demonstrated competency in both education and experience. FIRREA mandated licensing or certification pursuant to national standards, but the resulting regulatory structure has become tangled and overly complex. The system involves:

- Licensing and certification boards in all States and territories, each with differing interpretations of FIRREA, as well as differing agendas and funding;
- Minimum qualifications criteria established by the Appraiser Qualifications Board of The Appraisal Foundation, a nonprofit education organization;
- Appraisal standards (the *Uniform Standards of Professional Appraisal Practice*) established by the Appraisal Standards Board of The Appraisal Foundation; and
- Federal oversight by the Appraisal Subcommittee of the Federal Financial Institutions Examinations Council.

Unfortunately, FIRREA and its resulting complexity have adversely affected the appraisal profession and, in our view, put consumers, the States and the Federal insurance funds at risk. Much of the complexity was identified by the General Ac-

counting Office (GAO) in its investigation last year. We believe the problems are in four categories:

- Lack of accountability;
- Ineffective and counter-productive State enforcement programs;
- Minimum qualifications and discouragement of professional development; and
- Inadequate appraiser independence safeguards

The Multi-Pronged System Lacks Accountability

Title XI created the Appraisal Subcommittee to oversee the activities of the States and many of the activities of The Appraisal Foundation. The Appraisal Subcommittee is essentially a junior subset of the Federal Financial Institutions Examinations Council. The Appraisal Subcommittee funds a portion of The Appraisal Foundation's expenses. Ironically, individual State-certified and licensed appraisers fund the Appraisal Subcommittee operations through license fees collected by the States. Individual appraisers are assessed a $25 annual fee passed through to the Appraisal Subcommittee, which has amassed a sizable reserve fund for no identified purpose.

Effective Oversight of the Appraisal Subcommittee

We are concerned with the lack of oversight for the Appraisal Subcommittee. By and large, the Appraisal Subcommittee is operating in an insulated environment without any practical accountability measures.

Providing Federal oversight over an activity traditionally regulated by the States (licensing), the Appraisal Subcommittee is a hybrid Federal agency that has conducted much of its business in the dark and with no direct input from the appraisal profession. The Appraisal Subcommittee board is composed of staff bank examiners and program staff from the five Federal financial institution regulators and one from the Department of Housing and Urban Development. It meets quarterly in Washington, but does not allow for public access or participation to their activities and meetings.

The Appraisal Subcommittee staff performs audits of State appraiser boards on a 3-year rotation cycle, and works with State boards on Title XI compliance. The Appraisal Subcommittee posts some of the results of its audits on its website and a portion of this information is released in its Annual Report to Congress. Section 1103 of Title XI requires the Appraisal Subcommittee to issue an annual report to Congress no later than January 31 of the following year. The report itself historically has been little more than a financial statement, containing sparse information on the audits that were conducted with few compliance statistics. In addition, it is now nearly April and the 2003 Annual Report apparently has yet to be issued to Congress. Similar delays have occurred the past, like last year when the 2002 Annual Report was not issued until April 16.

Appraisal Subcommittee Oversight of States

Not only are the Appraisal Subcommittee's operations insular, but their powers are also impotent. Recommendations from the Appraisal Subcommittee are routinely disregarded by State appraisal boards, contributing to a cycle of ineffective enforcement. The only real power the Appraisal Subcommittee has over State appraisal boards is the authority to "decertify" a State if it is found to be out of conformance with Title XI. This specific power has generally become known as the "atomic bomb," because if it were to be invoked, virtually all mortgage lending in that State would cease. The Appraisal Subcommittee has never used this power, although it has threatened to do so. Such an unrealistic threat is an ineffective way to promote sound processes in the States.

According to the latest annual report issued by the Appraisal Subcommittee, a full 43 percent of the State appraisal regulatory agencies reviewed in 2002 either failed to resolve complaints against real estate appraisers expeditiously or were inconsistent in applying disciplinary sanctions; failed to pursue all alleged violations of the Uniform Standards of Professional Appraisal Practice; or did not adequately document enforcement-related files. In addition, one State failed to forward disciplinary actions to the Appraisal Subcommittee, which is required by Title XI and Appraisal Subcommittee Policy Statement 9. The fact that so many State appraisal boards failed to resolve complaints against appraisers in an expeditious manner is deeply troubling.

Examples of State appraisal board actions that have occurred without consequence from the Appraisal Subcommittee include:

- Hundreds of appraisers in Oklahoma who failed to meet the minimum requirements for licensing and certification were "grand-fathered" under a new licensing

law passed by the Oklahoma Legislature and endorsed by the Oklahoma Real Estate Appraiser Board Division;

- Failure of the New York Division of Licensing Services to revoke an appraiser's license following a guilty plea for "filing false documents," leading to 2 years probation and over $100,000 in fines and restitutions, because his certification would "not involve unreasonable risk to the safety and welfare of the general public." [1]
- Complaints against appraisers in multiple States that have gone unresolved up to 8 years.

Inadequate Structure and Regulatory Slights of Hand

In practice, FIRREA has weighed heavily on the development of appraisal practices in nonfederally related transactions, such as appraisal consulting and market analysis. When States implemented their FIRREA requirements for State licensing and certification, many of them wrote their laws to include all appraisal services performed in their State. These so called "mandatory" States require appraisals to be performed by licensed or certified appraisers and in conformance with the Uniform Standards of Professional Appraisal Practice. However, even in so called "voluntary" States, where nonlicensed or certified appraisers are allowed to "appraise" property, a de facto requirement to be licensed and certified exists. As a result, transactions outside of traditional mortgage lending are effectively being dictated by policies written and enforced by bank examiners (the Appraisal Subcommittee). We believe the Appraisal Subcommittee should have a more diverse membership since it will likely continue to impact practitioners delivering a wide range of appraisal and valuation assignments.

Finally, when implementing FIRREA, the five Federal financial institution regulators failed to take the licensing and certification requirement seriously. Through regulation, the law was effectively modified to exempt nearly 90 percent of all transactions in the residential mortgage market from being appraised by licensed and certified appraisers. As originally contemplated, all transactions greater than $15,000 would be required to be appraised by a licensed and certified appraiser, but with a regulatory slight of hand the threshold was raised to $250,000 before a licensed or certified appraiser was required. As a result, a significant portion of the real estate valuation work throughout the country takes place in the form of "evaluations," or "broker price opinions" (BPO's), or through "competitive market analysis" (CMA) reports. In many cases, evaluations are done by staff of organizations that have a vested interested in a real estate transaction. This negates the benefit of having an independent third party involved in the real estate transaction, while omission of a licensing or certification requirement for properties under $250,000 creates a disruptive gap in the enforcement of appraisal standards.

Ineffective and Counter-Productive State Enforcement

While there are many dedicated individuals on State appraiser boards, many times their ability to carry out their charge is compromised due to lack of funding or administrative support. Too often, complaints against real estate appraisers in States are not reviewed by State appraiser boards, leading to a lack of disciplinary action against poorly performing appraisers. Some State boards have been known to spend inordinate time and research and collect fines for inconsequential offenses, leaving little time for enforcement of major issues.

Concerns with State enforcement agencies include:

- Failure to review complaints in a timely manner or review them at all;
- Failure to apply appraisal review procedures consistently;
- Failure to proscribe disciplinary action against appraisers for poor performance; and
- Failure to provide adequate resources to investigate complaints as licensing fees are often commingled with the State's general fund and not used for oversight purposes as intended.

Neglectful Supervision and Administration

Since Title XI was enacted, it has been difficult to achieve necessary consistency among the States for enforcement of both standards and certification requirements. Whether through a lack of resources or a lack of will by those charged with providing oversight, the current system allows some unscrupulous and unqualified appraisers to continue practicing and has little or no recourse for their actions. In fact, some of these very appraisers have been linked to mortgage fraud schemes throughout the country.

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[1] Christian Murray, "Appraising the Appraisers," *Newsday,* August 9, 2002.

For example, within the last year, a real estate appraiser in New York was found guilty and convicted of a felony for grossly inflating appraisals. His State license was revoked, and he served a jail sentence for 1 year. Upon his release, he challenged the State appellate court to be regranted his license. The court overturned the ruling of license revocation, determining that he had served his time sufficiently and that he must return to becoming a "beneficial member of society." Amazingly, this fraudulent appraiser charged with participating in numerous land scam schemes is now a practicing appraiser—sanctioned—in New York.

New York is not alone in handling such cases carelessly, as a similar case was brought to light last month in Maryland. In June 2003, an appraiser who pled guilty to appraisal fraud admitted that the Government lost between $500,000 and $800,000 due to his actions. In the fall, he applied to renew his license. On the online application, he answered "no" to the question of whether or not he had ever been convicted of a felony. According to his attorney, he "honestly" answered no, because in the Federal system, one is not convicted until sentenced, and the appraiser was not sentenced until last month, in February. Thus, the Maryland Commission of Real Estate Appraisers and Home Inspectors renewed his license last October for another 3 years. A spokesperson for the Maryland Commission said to the *Baltimore Sun,* "all we have to go by is the honesty of the licensee. We are not required to perform background checks; moreover, the financial and personnel resources are not available at this time."[2]

Deficiencies with State appraisal complaint systems were noted in the GAO Report, most notably in relation to a Government Sponsored Enterprise (GSE) that recently began making referrals of poor appraisals to State appraiser boards. Eight hundred and sixty referrals were made to 45 different State regulatory agencies between August 2001 and August 2002. Officials from the GSE commented to the GAO that they had been dissatisfied with some State decisions on punitive actions and with the lack of feedback on actions that had actually been taken. The officials added that some States do not penalize appraisers for multiple violations if the appraisers have already been disciplined or do not tell complainants what action was taken. The officials reported that they have observed a lack of consistent and effective investigation and enforcement by some of the States. As an example, they noted that some States appeared to perform meaningful investigations and took appropriate actions while other States appeared unwilling to investigate similar cases with comparable support and documentation.

While FIRREA's complexity is causing problems with State enforcement, it is also placing a significant burden on appraisers working in more than one State. For example, a member of the Appraisal Institute from Virginia recently applied for a license in the State of Indiana. This individual is currently certified in Virginia, Maryland, New Jersey, West Virginia, Ohio, and Tennessee. After submitting the lengthy documentation on education and experience, the appraiser was notified that his application was to be tabled for 6 months due to his education not meeting their standards. This individual has taken virtually all of the courses offered by the Appraisal Institute and regularly teaches advanced curriculum courses across the country and in other countries.

Appraisers are paying a heavy price for redundant licenses while being denied others because of the bureaucratic nightmare created by FIRREA. A substantial percentage of real estate appraisers in this country are asked to perform real estate appraisal assignments that are not in their home State. This was not a major problem prior to the enactment of FIRREA; however, with its implementation each State must now take appropriate measures to facilitate the work of out-of-State appraisers who do business in multiple States. Our organizations believe that there are two appropriate methods for handling interstate appraisal work. The first method, "Temporary Practice," is mandated by Title XI, but unfortunately this fact was overlooked by many States and this provision of Title XI has not as yet been properly implemented throughout the country.

The second method, "Reciprocity," is not mandated by Title XI but in most cases will provide the maximum benefit to the public with the least amount of difficulty for the State regulators. In many parts of the country, the geographic areas for an appraiser's day-to-day business may lie within two or three States. In such cases, the "temporary practice" provisions are not appropriate to handle the appraiser's out-of-State business and the appraiser may be forced to become licensed or certified in two or more States. This means that several States may be required to administer the same process over and over again with no demonstrable benefit. In this situation, reciprocity agreements make a great deal of sense because they avoid du-

[2] John B. O'Donnell, "Real Estate Appraiser Faces Sentencing in Property Flipping Plot; Man Still Holds License Despite Pleading Guilty," *Baltimore Sun,* February 27, 2004.

plication of effort and, in doing so, lessen the administrative burden on each of the various States involved and the appraiser. To date, 12 jurisdictions have no reciprocal agreements in place, and those that do are not universal between all States. Virtually no new reciprocal agreements have been drafted since the early 1990's.

Minimum Qualifications and Discouragement of Professional Development

An important goal of FIRREA was to ensure that appraisals are performed by competent appraisers. However, in practice, FIRREA has had the opposite effect because it stresses minimum qualifications. This emphasis has severely curtailed the continuing development of a true appraisal profession.

This is explained well by users of appraisal services, who are in the best position to speak to changes in quality of appraisal services since the passage of FIRREA. In a poll conducted recently by the Appraisal Institute of significant users of appraisal services,[3] 50 percent responded that the quality of appraisal services and appraisal reporting has declined, whereas only 28 percent said appraisal services and reporting have improved. This is consistent with discussions our organizations have had with users of appraisal services for the past several years.

As we reflect upon FIRREA, it is clear that the requirements for licensing and certification were set too low. Unfortunately, many clients see the possession of a license to be the only necessary qualification and stop short of fully considering the issue of competency for a particular appraisal. Likewise, many appraisers feel it is enough merely to meet the minimum requirements. What the FIRREA legislation missed is recognition that attaining the minimum level of education and experience for a license or certification does not necessarily qualify the licensee as competent to appraise.

While our professional organizations maintain high standards and strict codes of ethics and effective peer review, less than 40 percent of all licensed and certified appraisers choose to be affiliated with such organizations. Currently, there are approximately 80,000 licensed and certified appraisers in the United States; out of this total; approximately 50,000 appraisers do not belong to professional appraisal organizations.

Those appraisers that have only met State licensing and certification requirements tend to be less experienced and qualified than appraisers with professional designations; 84 percent of users of appraisal services say this is the case. Ironically, after FIRREA was passed, our organizations saw appraisers retreat from professional organizations, as the Federal Government dictated that minimum levels were all that were necessary to perform appraisals in federally related transactions. As an example, in the case of the Appraisal Institute, from the early to late 1990's, membership dropped from over 35,000 members to slightly more than 16,000 members. The Appraisal Institute was not alone in this troubling circumstance.

Particularly problematic is a bizarre discrimination provision formulated against designated appraisers contained in Section 1122 of FIRREA, the "Anti-Discrimination" clause. This section states:

> "Criteria established by the Federal financial institutions regulatory agencies . . . for appraiser qualifications in addition to State certification or licensing *shall not exclude a certified or licensed appraiser for consideration for an assignment solely by virtue of membership or lack of membership in any particular appraisal organization.*"

In this case, the mischaracterized "discrimination clause" of FIRREA actually promotes discrimination against appraisers who have practiced appraisal for years and have achieved the highest credentials the industry offers. This section of FIRREA has been read to mean one need not be a member of a professional organization to be an appraiser. While this statement may be true, making such a statement is much like saying that consumers seeking medical care should not seek board-certified physicians or that a school prefers to hire people with GED's over those with Ph.D.'s. Fundamentally, it fails to recognize the intense work and diligence that thousands of professional appraisers have put into earning and maintaining their status as the most competent and experienced appraisers in the profession. The public and the real estate community should be aware that there are professional organizations that confer designations to appraisers who have advanced themselves significantly beyond the minimum requirements of FIRREA.

For decades it has been the professional organization and societies that have developed and maintained the basic principles and methodologies used by today's practitioners. Without professional organizations, the fundamental body of knowledge of

[3] "Appraisal Quality Post-FIRREA," A Survey of the Appraisal Institute's 2000–2004 Client Advisory Committee Members, March 21, 2004.

real estate valuation would not exist. To dismiss this segment of the lifeblood of the profession is a grave oversight with serious repercussions.

Inadequate Appraiser Independence Safeguards

While FIRREA did provide for some separation between real estate appraisal and loan production inside financial institutions, FIRREA failed to adequately address the issue of appraiser independence. Although Federal agencies issued the Interagency Appraisal and Evaluation Guidelines in 1994, recent bank examinations have indicated that this separation is failing to curb pressure to coax real estate deals along by influencing the independent judgment of appraisers. In October 2003, the five financial institution regulators issued an interagency statement reminding financial institutions that the 1994 Guidelines require that borrowers and loan production staff to not exert influence over the selection of appraisers. However, our members report that this is a regular occurrence. In fact, some financial institutions, mortgage brokers and others require a predetermined value to be met by an appraiser in order to receive future assignments from that institution. Such comments are often backed up by threats of coercion and nonpayment for services. FIRREA was established to avoid such circumstances, yet they are occurring every day under its purview.

There are relatively few options that appraisers have when confronted by inappropriate client pressure:

- First, the appraiser could turn down the assignment, or just say no. Many appraisers do this; however, given the dilution of the licensed appraiser market, our members report that it is likely that a financial institution will find an appraiser who is willing to bend to their request.
- Second, the appraiser could tell the individual ordering the appraisal that national uniform standards and State and Federal law require appraisers to perform assignments ethically and competently and that they would like to discuss and resolve any remaining concerns or issues. Appraisers and clients have such conversations on a regular basis, but appraisers are oftentimes faced with having to meet a predetermined value. This is particularly the case with many mortgage brokers and others whose compensation is driven by production.
- Third, the appraiser could report the activity to the appropriate enforcement authority. However, when doing so, the appraiser would have to ensure it was sent to the proper agency. Complaints against national banks would have to be sent to the Office of the Comptroller of the Currency; credit unions to the National Credit Union Administration, etc. Many parties, such as some mortgage brokers, are completely outside of a regulatory system. In these cases, the appraiser is simply forced to lose a client.

In some cases, bank examinations have uncovered unscrupulous activities. Oftentimes, the activities go unchecked an unreported. A particular problem appears to revolve around the fact that those who have a vested interest in the closing of the deal are ordering the appraisals. The 1994 Interagency Guidelines and the 2003 Interagency Statement call for a separation of loan production and credit analysis. However, full separation has never been realized, particularly in the areas of mortgage lending and brokerage. We believe that this is an inherent weakness of FIRREA that should be addressed immediately.

Legislative Recommendations

The Appraisal Institute urges Congress to explore the following suggestions as a starting point for addressing current deficiencies. These suggestions emphasize improving State appraisal board complaint processes, inserting accountability measures over the Appraisal Subcommittee and promoting consumer awareness and professionalism. Consider:

- Requiring the Appraisal Subcommittee to report to Congress annually their assessment of the effectiveness of each State's enforcement processes as part of their Annual Report, including results of all audits performed that year and a performance rating for all State appraisal boards.
- Requiring adequate funding for State appraisal boards for disciplinary functions enforced by the Appraisal Subcommittee.
- Modifying the makeup of the Appraisal Subcommittee to reflect broader representation, including an industry advisory council.
- Requiring the Appraisal Subcommittee to issue guidance to States addressing common deficiencies.
- Requiring the Appraisal Subcommittee to conduct public meetings.
- Requiring the Appraisal Subcommittee to consult and interview industry participants when conducting field reviews of State appraisal board operations.

- Requiring the Appraisal Subcommittee to share information from the National Registry with other Federal agencies, including the Federal Bureau of Investigation for antifraud purposes.
- Requiring the head of the Appraisal Subcommittee be confirmed by the U.S. Senate.
- Ensuring accountability of the Appraisal Subcommittee, and only then, providing it with authority to sanction consistent with its responsibility to monitor the activities of State appraisal boards.
- Granting the Appraisal Subcommittee authority for reciprocity of qualifications among licensing jurisdictions.
- Extending authority to the Appraisal Subcommittee for uniform temporary practice among licensing jurisdictions.
- Recognizing and encouraging the use of designated appraisers with qualifications beyond merely licensed and certified.
- Providing penalties for engaging in appraiser coercion and creating adequate resources for appraisers to report instances of such.
- Encouraging State appraiser boards to recruit the best qualified candidates to participate on board activities, regardless of membership in professional appraisal organizations.
- Requiring all regulated financial institutions to retain copies of all appraisals in loan files, even appraisals that are NOT used in the decision to lend.

Conclusion

There is an immediate need to find solutions to deficiencies in the system and our organizations are committed to assisting you in this effort. We look forward to working with you to identify solutions to solve the problems associated with the current appraiser regulatory structure.

PREPARED STATEMENT OF EUGENE KACZKOWSKI

PRESIDENT, AMERICAN SOCIETY OF APPRAISERS
ACCREDITED SENIOR APPRAISER, AMERICAN APPRAISAL ASSOCIATES, INC.

MARCH 24, 2004

Introduction

Chairman Allard, Ranking Member Reed, and Members of the Housing and Transportation Subcommittee, the American Society of Appraisers (ASA) greatly appreciates the opportunity to provide its views to the Subcommittee on "The Real Estate Appraisal Industry." We also appreciate the Subcommittee's interest in examining the impact of Title XI of FIRREA on the real estate appraisal profession, particularly with regard to protecting Federal financial interests and assuring the safety and soundness of real estate-related financial transactions in our marketplace. My name is Eugene Kaczkowski, and I serve as President of the American Society of Appraisers. I am an Accredited Senior Appraiser in the business valuation discipline and a Vice President with American Appraisal Associates, a full-service valuation consulting firm.

ASA is our Nation's only multidiscipline professional appraisal society that teaches, tests, and credentials its members in every major field of the appraisal profession, including residential property and commercial real property valuation; business enterprise valuation; machinery and technical specialties; and valuations of fine arts, antiques, gems and jewelry. Attached to my testimony is a fact sheet providing additional information on ASA.

Summary of Views

The American Society of Appraisers believes that the state of the real estate appraisal profession is generally good and that enactment of Title XI of FIRREA in 1989 was, and continues to be, an indispensable and positive force in professionalizing the Nation's real estate appraisers. We are convinced that today's real estate appraisers, as a group, are far better educated, more competent and are held to a higher standard of ethics and accountability than their pre-FIRREA predecessors. Having said that, ASA also believes that there are some serious problems in the regulated environment in which today's real estate appraisers function and that Title XI needs to be modernized and tightened in order to correct those problems.

The Pre-FIRREA World of Real Estate Appraisers

Before discussing these problem areas and recommending some approaches to addressing them, I would like to take just a moment to revisit the conditions that

made up the real estate appraisal industry prior to the enactment of Title XI. Pre-FIRREA, almost anyone could perform real estate valuations merely by declaring that they were competent to do so. At that time, there were few, if any, Federal requirements specifying the education, training, experience, and other skill sets necessary for an individual to estimate the market value of real estate collateralizing residential and commercial loans—sometimes totaling millions of dollars—made by federally insured financial institutions, guaranteed by Federal agencies like the FHA and VA or sold to investors in the secondary financial markets by the GSE's or their private sector counterparts. Only a handful of States had appraiser licensing programs of any kind. For the few that did, qualification requirements were inconsequential and nonlicensed individuals could continue to value real estate for virtually all transactions. These were the conditions that added billions of dollars in bailout costs to U.S. taxpayers when the savings and loan and banking industry crises occurred in the mid-to-late 1980's. What Congressional oversight committees, the General Accounting Office (GAO), and investigative reporters found when they examined the causes and consequences of the collapse was that in a shockingly large percentage of cases, the collateral for billions of dollars in defaulted real estate loans had been grossly overvalued by appraisers, sometimes because of incompetence and sometimes because they were pressured by lenders or developers to manufacture values sufficiently high to make the deal go.

An important component of Congress' package of responses to the debacle and to the role of faulty and fraudulent real estate appraisals was the enactment of FIRREA and its Title XI system of State appraiser certification and licensing.

What is Working in the Current Title XI System

ASA believes that there is much good public policy incorporated into Title XI. We think that the certification and licensing system correctly balances the interests and the roles of State and Federal Governments and the private sector in professionalizing real estate appraisers and making them accountable for their actions. Under the current system, States are responsible for certifying and licensing appraisers and for disciplining them when they are found to be incompetent or dishonest. Title XI invests in the not-for-profit Appraisal Foundation, which is responsible for promulgating uniform appraisal standards (the Uniform Standards of Professional Appraisal Practice or USPAP) and for establishing uniform qualification requirements for the certification of appraisers. Finally, because the integrity and accuracy of real estate appraisals impact so many important Federal programs and financial interests, Title XI leaves to the Federal Government, through the Appraisal Subcommittee, responsibility for overseeing the effectiveness of the State appraiser regulatory programs and standards-setting work of the Appraisal Foundation.

With a few noteworthy exceptions, which I will address, ASA believes Title XI's real estate appraiser certification and licensing system is working well. Today, there are more than an adequate number of State-certified and licensed real estate appraisers providing the uniform valuation services that are essential to our Nation's economy and to the cost-efficient operation of Federal programs. Under the current system, these appraisals are being performed in what we believe is a timely and cost-effective manner, utilizing valuation methodologies that are uniform across every region of our country.

What Needs Correcting in the Title XI System

Although we believe that Title XI is accomplishing its intended public policy purposes, there are some serious problems with the current system that ASA finds troubling and that we wish to bring to the Subcommittee's attention—including the failure of a small number of important Federal agencies to take advantage of it. Some of these problem areas fall within the clear jurisdiction of the Senate Banking Committee; others may require the attention of other Committees of the Congress. These are our concerns.

(1) Problem: The current membership of the Federal Appraisal Subcommittee is too narrowly drawn. The Subcommittee lacks representation from nonbanking and nonhousing Federal agencies that administer programs or have regulatory responsibilities that rely on the competency of real estate appraisers and the appraisals they perform. The Department of Interior (for example, land exchanges and sales, and conservation easements), the Department of Transportation (for example, right-of-way issues), the Internal Revenue Service (for example, charitable contributions of real estate and real estate assets in estate and gift tax returns) and the Securities and Exchange Commission (for example, financial reports of public companies where real estate holdings are material) are examples of Federal agencies whose activities regularly intersect the world of real estate appraisals.

Recommended solution: Although this issue needs to be analyzed in some depth, ASA believes that expanding the membership of the Appraisal Subcommittee would more accurately reflect the range of Federal interests in the work of real estate appraisers—and greatly maximize the benefits that the Federal Government receives from professional real estate appraisals.

(2) Problem: The Appraisal Subcommittee lacks appropriate rulemaking powers necessary to ensure that States regulate appraisers in a way that is uniform and fully consistent with Title XI requirements. Time and experience have demonstrated that the authority of the Appraisal Subcommittee to ensure compliance with Title XI needs to be enhanced. Under existing law, the Subcommittee only has two options with respect to its enforcement of Title XI: De-certifying a State's entire appraiser certification program or jawboning its licensing agency to take actions required to put it into Title XI compliance. Neither option is adequate. Rulemaking authority is a time-tested, fair and cost-effective way not only to ensure State agency compliance with Title XI requirements but also to ensure reasonable enforcement uniformity among the States (see Problem 3 below).

Recommended solution: Give the Subcommittee rulemaking authority.

(3) Problem: The regulation of appraisers by the States has been uneven. The regulation of real estate appraisers by the licensing boards of the 50 States, the territories, and the District of Columbia has been disturbingly uneven and, in some cases, borders on ineffectual. Title XI contemplated a reasonable degree of uniformity and certainty in the way States would enforce compliance with the ethics, competency and other protocols of professional appraisal practice. Based on reports from our real estate valuation members, this is not happening to an adequate degree.

Recommended solution: Ask the GAO, which did a good job fleshing out the landscape of Title XI's regulatory environment, to examine this issue and make recommendations on what States and the Federal Government need to do to improve the consistency and effectiveness of State compliance efforts.

(4) Problem: Improvements in State reciprocity agreements and temporary practice permits are required.

(a) Some States make the issuance of temporary practice permits difficult and very costly to obtain. Title XI recognized that real estate-related financial transactions requiring appraisal services are national (and often international) in scope, often requiring appraisers to travel from State-to-State on temporary practice assignments for a client. As a result, Title XI required States not to erect barriers to the issuance of temporary practice permits. Although local appraisers generally perform valuations of single-family properties in connection with mortgage financings, there are many instances in which national and regional mortgage lenders, real estate developers, insurance companies, and real estate investment trusts/partnerships hire major valuation firms or appraisers with a valuation specialty niche (for example, hotels, strip shopping malls, and office buildings) to appraise the market value of real estate in many States. Notwithstanding the efforts of the Appraisal Subcommittee to break down the barriers of some States to temporary practice, the problem remains.

Recommended solution: A consensus is developing between appraisers and major users of their services in support of a "driver's license" approach to temporary practice. Title XI should be amended to provide that appraisers duly certified or licensed and in good standing in one State must have their credentials honored in all other States for legitimate temporary practice purposes only.

(b) Reciprocity still needs improvement. In many areas of the country, real estate appraisers regularly practice on a multijurisdictional basis. The District of Columbia Metropolitan Area (DC, Maryland, and Virginia) is a typical example of a situation where an appraiser certified or licensed in one jurisdiction is likely to have clients in the other two jurisdictions. Because States frequently differ in their qualifications requirements for licensing or certification and because each State has its own fee structure, it is impractical and inefficient for an appraiser to obtain an original certification/license from each jurisdiction. Title XI contemplated easy reciprocity between and among States in situations where appraisers live and practice near borders with other jurisdictions.

Recommended solution: Title XI should be amended in a way that requires States to enter into mutually beneficial reciprocity agreements that facilitate interstate commerce.

(5) Problem: Because each State's appraiser licensing board currently must approve all primary and continuing education courses offered its licensees and licensee applicants, hardships are imposed on national education providers and practitioners. Professional appraisal societies offer their members and other qualified individuals a wide range of valuation course work. Providing continuing education to its members

from across the country is a central feature of ASA's annual conferences. The hardship on education providers is created when ASA—and other national appraiser education providers—must seek approval from each of the home States of its members in order for their continuing education credits to be accepted.

Recommended solution: A central clearinghouse should be established for the purpose of approving appraiser education course work for all States.

(6) Problem: The Appraiser Qualifications Board of the Appraisal Foundation lacks authority to establish qualification requirements for licensed appraisers in federally related transactions. An amendment to Title XI, approved approximately 2 years after its enactment, severely limited the authority of the Appraisal Foundation to establish qualifications for licensed appraisers in federally related transactions. The result is an anomalous public policy situation in which the foundation is able to establish qualifications for certified appraisers but not for the lesser-skilled licensed appraisers.

Recommended solution: ASA respectfully urges the Banking Committee to amend Title XI by restoring the foundation's authority to set minimum qualification requirements for licensed appraisers. The limitation on that authority was driven by a concern—among some mortgage market players—that the Qualifications Board would set qualification requirements so high that a shortage of appraisers would be created. Although that concern was highly dubious when it was made a decade ago, it has no validity today. Ironically, the concern today within the professional appraisal community and for many government officials is that qualifications for licensed appraisers in a number of States are inadequate. And, it is long past the time to end the illogical public policy disconnect between the Qualifications Board's authority to set standards for certified appraisers but not for licensed appraisers.

(7) Problem: The Federal bank regulatory agencies, by rulemaking, have limited the application of Title XI's professional appraisal and uniform standards requirements to loans above $250,000 for residential property and $1 million for commercial property. When Title XI was enacted in 1989, it included a de minis of $15,000. Although federally insured financial institutions and the GSE's are free to apply Title XI's provisions to transactions below the "de minimis" levels (and many do), ASA regards their establishment as unnecessarily jeopardizing "safety and soundness." The Uniform Standards of Professional Appraisal Practice permit certified and licensed real estate appraisers to tailor their services to meet their customers' needs as to speed and cost, without violating USPAP's ethics provisions. Accurate valuations of the collateral for loans by federally insured financial institutions are an indispensable safety and soundness component of a federally related real estate transaction.

Recommended solution: ASA urges the Banking Committee to request a GAO study of the de minimis issue, including an analysis of its safety and soundness consequences.

Conclusion

The American Society of Appraisers believes that the real estate appraiser certification and licensing system established by Title XI is working successfully to protect not only Federal financial interests but also the interests of consumers and the appraisal profession as well. ASA looks forward to working with the Senate Banking Committee to build on the current system for the purpose of strengthening it and correcting current weaknesses. I would be glad to answer any questions you may have.

Attachment

American Society of Appraisers: Fact Sheet

The American Society of Appraisers (ASA) is the only appraisal society in the United States that represents appraisers of all types of property—real, personal, and intangible. ASA has more than 6,000 professional members committed to providing consumers the best valuation expertise available. An international organization, ASA was founded in 1936 and is currently headquartered outside of Washington, DC, in Herndon, Va.

For nearly 70 years, ASA has fostered professional excellence.

- ASA accredits members only after they complete a rigorous testing and evaluation process that requires years of study, training, and peer review;
- ASA ensures that its accredited appraisers provide consumers and businesses with independent opinions of value;
- ASA provides continuing education programs and training opportunities to members;
- ASA maintains a strong role in the Appraisal Foundation, a nonprofit organization recognized by the U.S. Congress as the sole source for uniform appraisal standards and qualifications; and
- ASA requires all its members to subscribe to the Appraisal Foundation's Uniform Standards of Professional Appraisal Practice (USPAP) and ASA's Principles of Appraisal Practice and Code of Ethics, which the society enforces through a grievance process that allows clients to challenge appraisals rendered by ASA members.

ASA members come from all 50 States, Puerto Rico, the U.S. Virgin Islands, and 44 foreign countries (including Canada, Mexico, China, and the Philippines) and represent the following disciplines:

- Appraisal Review and Management: This discipline requires practitioners to manage multidiscipline appraisal practices, review appraisals performed by others and report the results of those reviews.
- Business Valuation (BV): Business valuation appraisers value intangible assets—patents, trademarks, copyrights, intellectual property; provide independent, unbiased opinions of values for businesses; and prepare merger and acquisition analysis and other studies. BV appraisers work for large accounting and financial consulting firms.
- Gems and Jewelry: ASA appraisers and Master Gemologist Appraisers assess every kind of gem and jewel, from mineral specimens and rough stones to art, designer, antique, and period jewelry.
- Machinery and Technical Specialties: Professional appraisers value machinery and equipment, cost surveys, aircraft, boats, oil and gas, mines and quarries, public utilities, IT property, and natural resources. They provide appraisals for Fortune 500 and other companies for the purposes of sale, acquisition, ad valorem tax, eminent domain, collateralization, or insurance.
- Personal Property: In this discipline, appraisers value art, antiques, books, automobiles, and residential contents, including every possible type of property from African sculpture to wines.
- Real Property: These appraisers may specialize in property that is urban, residential, ad valorem, rural, or timberland (including the land, improvements and all associated structures and additions). ASA appraisers can produce appraisals for acquisition or disposition, mortgages, insurance, estate taxes, etc.

Many ASA members are widely recognized experts and pioneers in their fields. They include:

- the founders of the business valuation appraisal profession, which comprises valuers of business and business interests of all sizes, from sole proprietorships to Fortune 500 companies;
- the personal property appraisers called on to appraise highly visible and valuable items such as gifts given to the First Family by foreign dignitaries and a collection of Princess Diana's dresses;
- the foremost expert in the field of "celebrity valuation," which involves appraising the value of a celebrity's brand and image along with his or her physical possessions;
- virtually all appraisers accredited in the appraisal of machinery and equipment and technical properties; and
- dozens of experts hired to appraise the value of the businesses, real property, personal property, machinery and equipment, and jewelry destroyed in the September 11 attack on the World Trade Center.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR REED FROM DAVID G. WOOD

Q.1. Do you believe that the Appraisal Subcommittee should have rulemaking authority? If so, why is that necessary and what do you see as the benefits?

A.1. During the review that resulted in our May 2003 report on the real estate appraisal industry, officials of the Appraisal Subcommittee stated that the lack of rulemaking authority, as well as limited enforcement powers, made achieving the uniformity and standardization, intended by Title IX, more difficult.[1] They further noted that allowing the Subcommittee to issue regulations would help ensure greater consistency among the States in credentialing appraisers and enforcing the most current version of the Uniform Standards of Professional Appraiser Practice. However, in commenting on our draft report, the Subcommittee stressed that the lack of additional authority has not been an impediment to achieving compliance with Title XI. Because our study did not encompass making independent assessments of compliance, we have no basis to question the Subcommittee's comments. However, our analysis of the Subcommittee's reports of its periodic field reviews—during which Subcommittee staff review the practices and activities of each State's appraiser regulatory organization—led us to recommend that the Subcommittee develop and apply clear and consistent criteria for assessing and reporting on State programs.

As we noted in our report, giving the Appraisal Subcommittee rulemaking authority would change the Subcommittee's role under Title XI from a monitoring to a regulatory function. This would have significant implications that Congress would need to consider. A fundamental question is who the Subcommittee would regulate and take enforcement actions against. For example, Title XI does not now mandate that States establish appraiser licensing or certification programs, but rather says that the States "may" establish such programs. (Obviously, by creating certain requirements for federally related transactions within the State, the Title gives the States a strong incentive to establish such programs.) Authorizing the Subcommittee to regulate and take enforcement actions against States could raise Constitutional questions.

Q.2. Do you believe that the Appraisal Subcommittee needs enforcement options other than decertification? If so, what specific measures would you recommend and why?

A.2. As noted in the response to question 1 above, officials of the Appraisal Subcommittee stated during our review that its limited enforcement powers made achieving the uniformity and standardization, intended by Title IX, more difficult. However, as noted, in commenting on the draft report the Subcommittee stressed that it has been able, within the existing statutory framework, to achieve compliance with Title XI. The Subcommittee further wrote it has been unable to identify other powers that would effectively improve its enforcement authority. We did not identify evidence indicating that the lack of additional enforcement authorities has adversely

[1] See U.S. General Accounting Office, *Regulatory Programs: Opportunities to Enhance Oversight of the Real Estate Appraisal Industry,* GAO–03–404 (Washington, DC: May 14, 2003).

impacted the Appraisal Subcommittee's ability to achieve compliance with Title XI.

Q.3. Mr. Fritts' testimony indicates that half of all appraisals originate with mortgage bankers and that Title XI does not regulate these appraisals. Do you believe that Title XI should be amended to capture appraisals originated by mortgage brokers?

A.3. Title XI was enacted primarily to protect federally insured depository institutions from losses and by extension the Federal deposit insurance funds. The term "mortgage bankers" is most often used to describe financial institutions that are not federally insured depository institutions. Mortgage brokers typically act as middlemen between borrowers and lenders; the lenders may or may not be federally insured depository institutions.

Title XI requirements are applicable to all federally related transactions entered into by a federally insured depository institution, whether or not they involve mortgage brokers. As such, the central issue is whether the appraisal standards and appraiser qualifications that Title XI requires for federally related transactions should be extended to real estate mortgage transactions entered into by non-federally insured depository institutions.

GAO has previously identified issues and concerns with respect to Federal oversight of non-federally insured mortgage lending institutions, most recently in our January 2004 report on predatory lending.[2] However, amending Title XI to cover appraisals used in transactions by non-federally insured mortgage lending institutions—including their transactions involving mortgage brokers—would represent a fundamental shift in focus. Title XI would not have strictly the purpose of protecting the Federal deposit insurance funds, but rather a broader consumer protection aspect. This would likely raise additional Federal-State jurisdiction issues, as mortgage bankers and brokers are licensed and supervised by the States. Such a change would also raise issues of implementation and enforcement. Currently, Title XI requirements in effect apply to the depository institutions that are federally supervised; the requirements are implemented through regulations that the five Federal financial institution regulators promulgate and enforce. It is unclear who, using what means, would enforce requirements among lenders that are not currently supervised by Federal regulators.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR REED FROM CHARLES CLARK

Q.1. Do you believe that the Appraisal Subcommittee should have rulemaking authority? If so, why is that necessary and what do you see as benefits?

A.1. The Board does not believe that the responsibilities of the Appraisal Subcommittee as currently outlined in Title XI warrant rulemaking authority. Their responsibilities are clearly outlined in the law and require no special interpretations by rule. Only if Title XI were amended to give the ASC final authority over the criteria

[2] U.S. General Accounting Office, *Consumer Protection: Federal and State Agencies Face Challenges in Combating Predatory Lending,* GAO–04–280 (Washington DC: January 30, 2004).

for appraisers and the standards for appraisals would they have need for rulemaking authority.

Further, the Board believes that the ASC has successfully discharged its fundamental requirements under Title XI to oversee the development of State regulatory programs and the creation of the Uniform Standards of Professional Appraisal Practice. Thus, Congress should sunset its operations.

Finally, as the GAO report notes, giving the ASC rulemaking authority would convert it from a monitoring agency to a regulatory agency. Doing so, could result in court challenges to the Federal Government's overstepping the Constitutional limits of the Tenth Amendment.

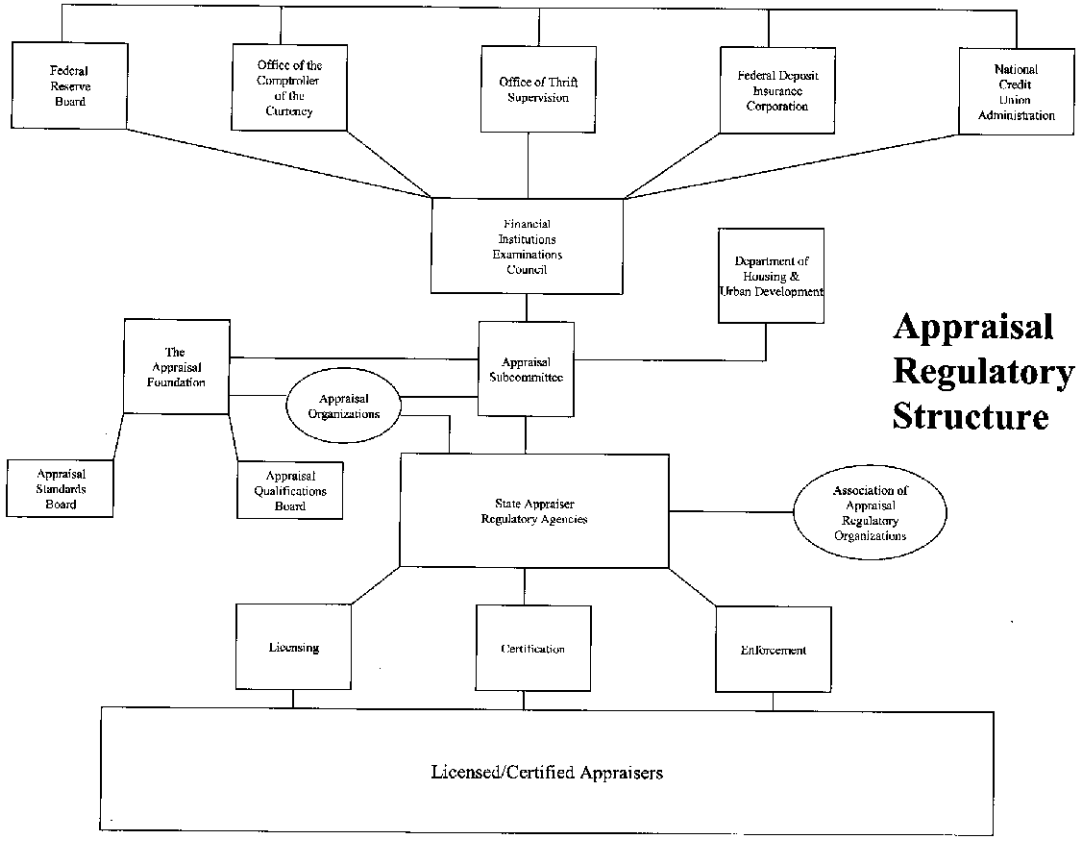
Q.2. Do you believe that the Appraisal Subcommittee needs enforcement options other than decertification? If so, what specific measures would you recommend and why?

A.2. No. As the ASC indicated in its response to the GAG's 2003 Study, they could identify no other "powers that would effectively improve their enforcement authority." We concur. Their reviews of State operations and policy of issuing statements appear sufficient.

Q.3. Mr. Fritts' testimony indicate that half of all appraisals originate with mortgage bankers and that Title XI does not regulate these appraisals. Do you believe that Title XI should be amended to capture appraisals originated by mortgage brokers?

A.3. To the extent that a mortgage broker is acting on behalf of a lender regulated by a member of the Federal Financial Institutions Examination Council, the Georgia Board believes that they are regulated by the provisions of Title XI. If the mortgage broker is working for a lender not regulated by a FFIEC member, then the mortgage broker should not be covered by Title XI.

Appraisal Regulatory Structure



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CHARLES CLARK
Real Estate Commissioner

April 5, 2005

The Honorable Wayne Allard
United States Senate
525 Dirksen Senate Office Building
Washington DC 20510-0606

Dear Senator Allard

The day after your Subcommittee held its hearing regarding Title XI's Appraisal Reform Amendments, David Bunton sent a memorandum to sixteen states stating that I had identified them as supporting the Georgia Board's proposal to sunset the Appraisal Subcommittee (ASC).

After getting and reading the Subcommittee's official transcript, I can understand how one could read my testimony to mean that I was naming States that had formally supported our position. In response to a question from Senator Miller asking what other States supported our position, I cited the GAO's statistical data reflecting that 23 States would sunset the ASC and then said "In terms of the States that I am aware of, people that I have personally spoken to, regulators in the following states tell me that they support our position [I then listed the 16 States]. . . regulators in all of those States have indicated to me personally that they support our general position."

I would like to take this opportunity to clarify my remarks regarding the position of other states appraiser regulatory agencies. My intent was not to give the official position of any state other than Georgia. I did not intend, and was not intending, to represent that any of those States' appraiser regulatory boards has taken a formal position with respect to the GAO Report. I was only responding to a question posed by Senator Miller and indicated that I had personally spoken with individual regulators in 16 states that told of their individual support for Georgia's general position. While we hope that other States will endorse our position, so far as I know they have not done so to date.

Senator Allard
April 5, 2004
Page 2

I appreciate the consideration shown to me and my colleagues by the Subcommittee and would be glad to provide any additional information for the Subcommittee's consideration.

For the Board

Charles Clark
Real Estate Commissioner

CC/amf

cc: Senator Zell Miller
Senator Jack Reed
Regulatory Agencies of the Sixteen States

Enclosure Pages 54 & 55 of Transcript

STATEMENT OF
FRANCOIS K. GREGOIRE
CHAIRMAN, FLORIDA REAL ESTATE APPRAISAL BOARD
TO THE U.S. SENATE
COMMITTEE ON BANKING, HOUSING and URBAN AFFAIRS
SUBCOMMITTEE ON HOUSING and TRANSPORTATION
REGARDING
THE REAL ESTATE APPRAISAL INDUSTRY and TITLE XI of the
FINANCIAL INSTITUTIONS REFORM, RECOVERY and ENFORCEMENT ACT of 1989
MARCH 24, 2004

Mr. Chairman, Members of the Subcommittee, as Chairman of the Florida Real Estate Appraisal Board, this opportunity to submit written testimony regarding the Real Estate Appraisal Industry and Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) is appreciated. Florida has over 5,300 Licensed and Certified Appraisers and almost 7,300 Registered Trainee Appraisers. The State of Florida regulated appraisers and appraisal practice long before Title XI of the Financial Institutions Reform Recovery and Enforcement Act of 1989 (FIRREA) and was one of the first jurisdictions to enact a real property appraiser licensing and certification law in an attempt to comply with the Federal Mandate.

The Subcommittee is to be commended for this examination the effectiveness of the current federal and state regulatory structure set forth in Title XI of FIRREA. The General Accounting Office's (GAO) report on enhancing oversight of the real estate appraisal industry merely scratches the surface in revealing the challenges faced by State Regulatory Agencies in meeting their obligations under FIRREA. The GAO report reveals Federal, state and private entities are combined to form an overly complex and convoluted structure charged with the responsibility of protecting the interests of Federal Financial Institutions. Agency regulatory officials, professional associations, mortgage industry representatives, the Department of Housing and Urban Development and government-sponsored enterprises such as Fannie Mae and Freddie Mac all raised concerns about the regulatory structure created by Title XI. Due to the complexity of this structure and the multitude of participants, the GAO Report, unfortunately, failed to examine in detail many of the problems experienced by the States and neglected making any substantive recommendations for improvement or change.

WHAT DOES WORK IN FLORIDA:

- **Florida's Certification and Disciplinary System**

Florida does evaluate, approve and disapprove prelicensing courses for appraisers. We receive applications, evaluate an individual's appraisal education and experience, along with their background and make a determination if they are competent and qualified to make real estate appraisals with safety to those whom they may undertake a relationship of trust and confidence and the general public. Florida does deny individuals licensure for a variety of reasons, including prior criminal history. Florida does administer a Certification Examination, approved by the Appraiser Qualifications Board for both Residential and General Appraisers. Appraiser Credentials are issued to Registered Trainee Appraisers, State-Certified Residential Appraisers and State-Certified General Appraisers. Over 1,500 new credentials for our three categories of regulated appraisers were issued in 2003. Florida evaluates applications for Temporary Practice Permits from individuals with appraiser credentials from other jurisdictions. Over 130 of these were granted in 2003.

Florida does evaluate, approve and disapprove continuing education course offerings, including those provided by means of distance learning, and require regular continuing education of their licensees. Florida has an electronic license renewal program to ensure 100% compliance with required appraiser continuing education.

The Florida Real Estate Appraisal Board receives complaints alleging violations of our statute, rules of the Florida Real Estate Appraisal Board and the Uniform Standards of Professional Appraisal Practice (USPAP). Over 350 complaints were processed in 2003. The complaints were investigated and prosecuted when deemed to be legally sufficient and with probable cause.

When found guilty, appraisers have been sanctioned for violations of Florida law, Rules of the Board and the USPAP. Over the past year, these included remedial education, fines, suspensions of licenses and license revocations.

Although each regulatory jurisdiction faces challenges, an examination of the three most recent Appraisal Subcommittee Annual Reports to Congress seems to indicate most are fulfilling their responsibilities. The most serious concern expressed by the ASC is the failure of States to submit roster and disciplinary reports in a timely manner and tardiness in the remittance of National Registry fees. In fact, over the past three years, the only suspensions of the ASC's recognition of a jurisdiction's appraisal certification program were not due to any allegations of failure to enforce standards or ensure real property appraisers met qualification criteria. One was due to a state's failure to submit roster information, and fees in a timely manner. The other was due to a state's inability to submit their appraiser certification examination to the AQB for scrutiny and comparison to a new subject matter content matrix.

- **Florida's Professional Appraisal Associations**

The Professional Appraisal Associations in Florida continue to offer high quality educational programs for their members and non-member appraisers. These Associations, the Appraisal Institute, the National Association of Independent Fee Appraisers, the American Society of Appraisers, the National Association of Master Appraisers, the American Society of Farm Managers and Rural Appraisers and the National Association of REALTORS, all Appraisal Sponsors or Affiliate Sponsors of the Appraisal Foundation develop pre-licensing, post licensing and continuing education courses which are high quality and intended to develop individuals into ethical and competent real property appraisers.

Each of these organizations endeavors to communicate changes in the law, changes in policy and rules changes to their members and encourages involvement in the regulatory process. Each has a Code of Ethics which embraces and enhances the Uniform Standards of Professional Appraisal Practice. These professional associations encourage members to mentor, train and guide new members of the profession and provide wholehearted support of the regulatory program in Florida.

WHAT DOES FLORIDA PERCEIVE AS PROBLEMS WITH CURRENT STRUCTURE?

- **USPAP Is a Moving Target**

Title XI of FIRREA requires each Federal financial institution's regulatory agency and the Resolution Trust Corporation to prescribe appropriate standards for the performance of real estate appraisals. At a minimum the rules must require that real estate appraisals be performed in accordance with generally accepted appraisal standards. These are the appraisal standards promulgated by the Appraisal Standards Board of the Appraisal Foundation

Additionally, Title XI states a time limit for adoption of the standards in final form along with a time limit for an effective date.

The reality is the USPAP is far from final. For each of the last six years (and most likely longer) there have been changes to these "standards". In addition to their regulatory responsibilities, Board Members, Prosecutors and financially strapped administrators must regularly monitor the Appraisal Standards Board for their regular Exposure Draft of proposed changes to the USPAP. Valuable time is consumed examining the changes and drafting responses and suggestions for revision. Rarely do jurisdictions have either the funds or the personnel available to attend the far flung public meetings to provide public comment and make their points in person. Like clockwork, however, changes will be adopted by the ASB and must then be implemented and enforced by the regulatory body.

Floridians are fortunate our appraisal statute is written in such a way these changes to the USPAP are automatically effective. The GAO study reveals, however, 50% of the jurisdictions take at least one month to adopt changes, 30% take over four months and

some jurisdictions take over twelve months. In fifteen states, the legislature must formally adopt changes to the USPAP prior to implementation.

How can there be effective and uniform enforcement if the standards of appraisal practice are nearly never stable and states are employing different versions of the "standards?" The GAO study reveals 70% of the states believe their ability to regulate appraisers would be enhanced if the USPAP was updated less frequently. Only three states believed it would hinder their effectiveness.

The existence of Uniform Standards of Professional Appraisal Practice is clearly necessary for the protection of the interests of Federal Financial Institutions and the public. Appraisal practitioners, professional appraisal organizations, mortgage loan originators, secondary lenders, investors and state regulators seem to be in agreement on this one issue. The other notable point of agreement is, to be effective, the standards must be fixed for a period of more than one year.

- **The Appraiser Qualifications Board routinely expands their authority**

Tittle XI mentions the Appraiser Qualifications Board in only two paragraphs and provides **only two** specific responsibilities. These are to establish the **minimum** criteria for appraiser certification and to issue or endorse a State Certification Examination or determine the equivalency of a State Administered Examination.

The AQB, however, has gone far beyond establishing minimum criteria. Requirements for regular continuing education have been established, not only for the number of hours, but course content and specific courses of instruction. The AQB has taken upon themselves the role of a regulatory agency by establishing a course approval program, and disapproving a number of already state-approved pre-licensing and continuing education courses because of minor technical differences and have imposed their own arbitrary criteria.

The AQB has mandated a specific course, the 15-Hour National USPAP Course, or its equivalent, as a prerequisite to appraiser certifications. The course must be taught by an AQB Certified Instructor. The AQB Certified Instructor must have completed and AQB Certified Instructor Course and Examination, must attend the AQB mandated Certified Instructor Continuing Education and must use the AQB course materials. Of course, these must be licensed, **for a fee**, from the Appraisal Foundation. The AQB Certified Instructor has the option of offering an equivalent course. Only the AQB can determine equivalency. **There is no appeal and no appeal entity**.

Florida believes it is a clear conflict of interest for the AQB to mandate a specific course of instruction, taught only by their credentialed instructors, with a financial benefit to the Appraisal Foundation.

The Certification of Instructors is clearly beyond the realm of duties envisioned in FIRREA. Just today, the Appraisal Foundation issued a Certified USPAP Instructor Bulletin (copy attached). The mandates of required completion dates, specific course

effective dates, rules for tracking forms and Instructor Rectification Forms not only conflict with many State's rules and policies, they insult the capabilities and mission of state regulators.

Also announced in the bulletin is the "Certified Instructor Complaint Process." This is but another example of the AQB expanding their authority.

For over two years, the AQB has been on a quest to rewrite the Appraiser Qualifications Criteria. To make the criteria more robust. More stringent. More difficult. This, despite the fact the GAO survey of the States indicates less than 17% of the regulatory agencies believe the current education and experience required is inadequate. This, despite the fact the GAO found no problem with the level of education and experience required. Although the level of education and experience required under current standards is not mentioned as a problem in the last four ASC Annual Reports to Congress, the AQB more stringent standards are imperative to enhancing public trust in the appraisal profession.

FIRREA specifically permits any Federal agency to establish additional qualification criteria for appraisers to carry out the statutory responsibilities of their department or agency. Not one agency has done so. Yet the AQB insists the current Appraiser Qualification Criteria is insufficient. It's clear the AQB sees an opportunity for an income stream.

- **Autonomy and Secrecy of the ASB and AQB**

Members of the Florida Real Estate Appraisal Board are appointed by the Governor subject to confirmation by the Senate. In addition to State Ethics and Financial Disclosure requirements, Florida mandates open meetings with ample public notice and opportunities for public comment. The Appraisal Subcommittee has adopted a Policy Statement to guide the actions and behavior of Regulatory Board Members (Statement 1). Members of the ASB and AQB are not subject to any such requirements.

According to the bylaws of the Appraisal Foundation, the AQB and the ASB are autonomous. Members are appointed by the Board of Trustees of the Appraisal Foundation and subject to no government rules. States, especially Florida, question the propriety of a private, autonomous boards promulgating standards for appraisals and qualifications of appraisers, which must then be adopted and enforced by the State regulatory agency. These standards and criteria have the effect of law but they have been adopted completely outside the State legislative process.

Although the standards and criteria are issued for public comment, they are nonetheless discussed, debated, decided and mandated by independent and autonomous Boards of the Appraisal Foundation in non-public meetings. Rules, regulations and standards enforced by a state regulatory agency should be enacted under the same laws, rules and guidelines applicable to that agency.

Nearly 70% of the States surveyed by the GAO believe all meetings of the ASC, ASB and AQB should be open to the public.

Decisions made by the private ASB and AQB often require State Legislatures to enact or amend laws. As stated previously, each change of the USPAP by the ASB requires legislative action in 30% of the states.

The AQB just this year adopted a new, more stringent and restrictive Appraiser Qualification Criteria. Although not all states have been surveyed, this decision will require the Florida Legislature to make amendments to our appraiser certification statute to implement. It appears to be the epitome of arrogance for an unelected, autonomous, private group, answerable to none, to command a State Legislature to act or risk some sanction imposed by the heavy hand in Washington, D.C.

Among the responsibilities of the Appraisal Subcommittee is to review the practices, procedures, activities and organizational structure of the Appraisal Foundation, the ASB and AQB. However, the Appraisal Subcommittee often remains silent and thus conveys the impression that they are working in concert with the Appraisal Foundation and the members of its ASB and AQB. In part, this may explain why **only 30%** of the states, according to the GAO, believe eliminating the oversight role of the ASC would hinder their ability to regulate appraisers.

- **Less Than Ideal Relationship with the Appraisal Foundation**

Although the Executive Director of the Appraisal Foundation and members of both the Appraisal Standards Board and the Appraiser Qualifications Board routinely attend meetings of the Association of Appraiser Regulatory Officials (AARO) to provide updates and information, and have provided training programs for State Regulators, the relationship is far from rosy in all jurisdictions. Due to acrimony which developed during an AARO meeting in 2002, some ASB, AQB and ASC representatives were heard to vow never to attend another meeting of the regulatory group.

In an attempt to heal the rift, the Appraisal Foundation created the State Regulator Advisory Group. When some States attempted to place their entire board on that panel, the Appraisal Foundation limited each state to no more than two members. Just over on half, (twenty nine) of the regulatory jurisdictions are represented on the State Regulator Advisory Group. Fewer attend the meetings.

In addition to the State Regulator Advisory Group, the Appraisal Foundation has other advisory councils. All but the State Regulator Advisory Group are featured on the Appraisal Foundation website. The functions of each are outlined and explained. Unlike the other Appraisal Foundation advisory groups and councils, the State Regulator Advisory Group does not choose its own leadership, it does not choose its meeting dates and does not set the agenda. Although participants have been able to provide comment and suggestions, as well as air their grievances, the meetings are orchestrated to benefit the Appraisal Foundation.

- **Failure to Report Underperforming Appraisers**

The GAO identified one of the main problems State Regulators encounter in fulfilling their FIRREA responsibilities. Many of the Federally regulated institutions have made a conscious decision not to make referrals or complaints to the State Regulatory Agency. Some representatives of Government Sponsored Enterprises have made public statements of their unwillingness to file complaints. Fannie Mae, within the past two years, made a very public decision to refer problem appraisers to the appropriate State Regulatory Agencies, and followed up with very public comments their complaints were not immediately resolved, or that they were asked for supplementary information which inconvenienced them.

It could be the market is working the way some expect it to work. When consumers of appraisal services find an unethical appraiser, they make a decision to refrain from using his services. There are a number of "do not use" lists circulating. This may be a less expensive and less cumbersome means to let this market regulate itself.

WHAT WAS NOT STUDIED BY THE GAO?

- **Lender Pressure on Appraisers**

FIRREA was enacted in reaction to a collapse of the United States Savings and Loan Industry. The Congressional Testimony and debate preceding its enactment reveals story after story of the pressure imposed on appraisers by regulated lenders pressuring appraisers for documents to support their lending decisions. In many of those cases, the decision about the loan was a foregone conclusion; the lender merely needed "something for his file". Nowhere in FIRREA is this root cause of unethical practice addressed and at no time has there been any Federal initiative to address this very real problem. Some Federal agencies have adopted policies with respect to Appraiser Independence in an attempt to thwart **borrower** influence and pressure, but **lender** and **loan originator** pressure is either ignored or swept under the rug.

Since the advent of Federally mandated appraiser licensing and certification, the problem of pressure on appraisers has not disappeared. If anything, it has become more pervasive and widespread. Prior to the 1980's a high percentage of mortgage loans were made by local institutions with local money. Since then, secondary mortgage lenders have taken over as the leaders in holding these instruments. In this Internet age, it's common for the borrower to never meet the loan originator and to secure a mortgage loan from a company in another state or from across the country.

During 2003, a company by the name of October Research, conducted a survey of appraisers in 44 states on a variety of subjects including lender pressure. Their research revealed, 55% felt pressure to overstate home values and nearly all of the respondents said some of their peers "sometimes go along" with such pressure. A

recent article in the American Banker (attached) supports the research data on appraisal pressure. The American Banker reported that in personal interviews with appraisers across the country, appraisers uniformly indicated that the pressure increased during the recent refinancing boom as brokers and lenders scrambled to get consumers top cash out privileges for their refi efforts. One North Carolina appraiser reported being "blacklisted," and losing 60-70 % of his business over the past several years, because he refused to inflate appraisals to meet loan broker's goals. He reported in his area, foreclosures have doubled, largely due to hollow appraisals that artificially inflated property values in recent years

Pressure on appraisers is often exerted by individuals involved in property flipping and predatory lending. Many of these mortgage loans, sold to Fannie Mae and Freddie Mac, are originated by individuals and companies with no stake in anything other than the loan closing. The lack of oversight of the mortgage loan origination segment of the market has an adverse effect on the ability of appraisers to do their jobs effectively and ethically.

For the past couple of years an "Appraiser's Petition" has been posted on a well known Appraisal Website. It succinctly describes the everyday pressure and tactics employed against appraisers. Over 7,600 Appraisers have electronically affixed their signatures to this document. This petitions has been supplied to the Appraisal Subcommittee on more than one occasion. It does not appear any progress has been made on the issues raised. A copy is attached for your reference.

CONCLUSION

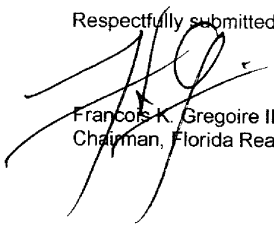
It's clear oversight of the appraisal regulatory structure should be geared toward the interests of consumers and the protections the consumer should expect from an independently developed, unbiased, objective third party opinion of value of the real property offered as security for a loan. The Uniform Standards of Professional Appraisal Practice (USPAP) need to be stable and final. Appraiser Qualifications have been established and should be enhanced only by Federal agencies or Instrumentalities if deemed necessary. The conflicts of interest apparent in the activities of the Appraiser Qualifications Board should be eliminated.

The Appraisal Subcommittee should spend less of its time nit-picking the states on minor technical issues and registry fee collections and make a simple determination if the jurisdiction has created an appraiser licensing and certification program in accordance with FIRREA. It could be their job is done in that area.

The vast majority of appraisers in this country are honest and ethical. They endeavor to perform their responsibilities according to generally accepted practices (USPAP) and are worthy of the public trust. However, as recent studies reveal, all deal daily with pressure from unscrupulous market participants. Congress must address the issue of pressure on appraisers.

This opportunity to share views, observations and suggestions is appreciated. Be assured the members of the Florida Real Estate Appraisal Board stand ready to work with the Subcommittee to improve effectiveness of the current federal and state regulatory structure as set forth in Title XI of FIRREA.

Respectfully submitted,



Francois K. Gregoire IFA RAA
Chairman, Florida Real Estate Appraisal Board

THE APPRAISAL FOUNDATION
Authorized by Congress as the Source of Appraisal Standards and Appraiser Qualifications

CERTIFIED USPAP INSTRUCTOR BULLETIN

The following is an update for AQB Certified USPAP Instructors. It contains current policies and important reminders. As always, any questions regarding the Certified Instructor Program may be directed to Mavis Kleso by e-mail at mavis@appraisalfoundation.org or by calling (202) 624-3050.

National USPAP Courses

The Appraisal Foundation recognized a need to facilitate the transition from one edition of *National USPAP Courses* to another, and to allow additional time for course providers to obtain course approval from their state(s). As a result, Foundation policies currently allow *National USPAP Courses* to be offered once published by The Appraisal Foundation in the fourth quarter of the preceding year, and in the first quarter of the following year. Please see the following table regarding 2003, 2004 and 2005 *National USPAP Courses*:

National USPAP Course Edition	May Be Offered Beginning	Must Be Completed By	Student Tracking Forms Due
2003	1/1/2003*	3/31/2004	4/30/2004
2004	Once published by The Appraisal Foundation in the 4th quarter of 2003	3/31/2005	4/30/2005
2005	Once published by The Appraisal Foundation in the 4th quarter of 2004	3/31/2006	4/30/2006

*Policy allowing course validity in the 4th quarter of the preceding year did not exist until 2003

- As indicated above, **all course work and examinations must be completed by March 31**. This includes examinations and re-takes.
- As always, the student tracking forms must be submitted within 30 days after the course offering. Therefore, any tracking forms received after April 30 (for a preceding year course) will **NOT** be accepted or processed.
- For prior year courses being offered in the first quarter of the current year (i.e. offering the 2004 course in February 2005), students **must** be provided with a copy of the Appraisal Standards Board's *Summary of Actions*, showing the changes to USPAP for the current year (in this example, changes effective for the 2005 USPAP).

The Appraisal Standards Board hopes to move to a two-year USPAP revision cycle (instead of annually) within the next few years. When that occurs, *National USPAP Courses* will only be valid through December 31 (of the second year).

Continuing Education Requirement

To satisfy the 7-hour *National USPAP Update Course* continuing education requirement, the 15-hour *National USPAP Course* may be taken **in 2003 and 2004 only**. Commencing in 2005, students will no longer be able to take the 15-hour course in lieu of the 7-hour course.

When taking the 15-hour course in lieu of the 7-hour course, the state licensing jurisdiction must determine whether the student is required to take and pass the associated examination.

Instructor Recertification Courses

The certifications of instructors who were certified in 2002 originally had an expiration date of December 31, 2004; however, that expiration was subsequently extended to June 30, 2005.

Instructors whose certification expires in 2005 will be required to attend a 7-hour Instructor Recertification Course, but **will not be required to complete an examination** as part of this recertification process.

Although testing will not be performed for this cycle, the AQB has reserved the right to conduct examinations in future recertification courses based on the passage of time, or when significant changes in USPAP are made.

Instructor Recertification Courses will commence in late 2004. Dates and locations will be announced within the next few months.

National Student Tracking Database

The Appraisal Foundation now has a National Student Tracking database online for use by state regulatory officials. Although many states will continue to require course completion certificates and transcripts from schools and instructors, this new tool is designed to assist states in verifying that a student completed a *National USPAP Course*, taught by an AQB Certified USPAP Instructor, and a state certified appraiser. State regulatory officials may request a User ID and password to access this secure database by contacting Ericka McLeod via email at Ericka@appraisalfoundation.org or by calling (202) 624-3054.

Certified Instructor Complaint Process

The AQB Certified USPAP Instructor Complaint Process is now established. Complaints submitted to The Appraisal Foundation will be screened and evaluated to determine whether or not an investigation is warranted. If an investigation is deemed warranted, the Respondent (instructor) will be notified and will be given full opportunity to address the allegations in the complaint. The matter would then be reviewed by a committee that consists of a member of the Appraisal Standards Board, the Appraiser Qualifications Board, and a senior Foundation staff member. If the committee finds that violations occurred, it may issue:

- A private letter of warning/reprimand, with or without conditions;
- A suspension with or without conditions for up to one year, with publication; or
- Revocation of certification with publication.

After notification of a sanction, the Respondent may appeal the sanction (but not any underlying findings of fact) to the Appraiser Qualifications Board within 30 days.

Other Information

- Please remember that it is the policy of the Foundation to grade the examination only on a pass/fail basis. "Raw scores" or other data must never be provided to the student.

- A downloadable version of USPAP is available from the Foundation for $24.95. Many instructors have indicated that it is a very valuable tool to have when instructing a class and using a PowerPoint presentation.

- The Appraisal Standards Board will hold public meetings on: April 6th in San Diego, California; June 15th in Kansas City, Missouri; and October 8th in Washington, D.C. The Appraiser Qualifications Board will hold public meetings on: April 23rd in Cincinnati, Ohio; July 23rd in Oklahoma City, Oklahoma; and on October 8th in Washington, D.C.

A View of Refi Boom Pressures From the Appraisal Trenches

From: American Banker

Thursday, February 5, 2004

By Jack Bergquist

Home appraisers are usually selected and paid by commissioned loan officers and mortgage brokers, who have an incentive to close as many loans as possible for the highest amounts possible.

So it is almost inevitable that some appraisers would complain about pressure from originators to overstate property values. But several appraisers interviewed by *American Banker* said such pressure intensified during the refinancing boom of the last three years.

As more consumers sought to take equity out of their homes, the appraisers say, loan officers and mortgage brokers increasingly leaned on them to come through with values high enough to make cash-out refis worthwhile. If the appraisers held their ground, they said, they lost business to others who did not.

The perception appears to be held by appraisers nationwide, in both hot and lukewarm real estate markets.

Of the 500 appraisers October Research Corp. surveyed last year, 55% said they felt pressure to overstate home values. And nearly all the respondents said at least some of their peers "sometimes go along" with such pressure.

October, of Richfield, Ohio, conducted the survey from April through December. It polled appraisers in 44 states. The number surveyed in each state was proportional to the percentage of the nation's appraisers who were licensed in that state, according to Joe Casa, October's publisher.

This was the firm's first national survey on appraisers, Mr. Casa said, but many appraisers told October "it's much worse today than it's ever been."

Some critics have gone as far as to suggest that pumped-up appraisals heighten the danger of a national housing bubble. At the very least, lenders

that sell mortgages into the secondary market risk being forced to buy defaulted loans back if the appraisals were overstated.

Searching For Solutions

Consumer activists have called appraisal inflation a predatory practice. Trade groups, including the Appraisal Institute in Chicago, have tried to call attention to the issue, and Congress has taken a look as well.

"Our members have told us that appraisers experience inappropriate pressure to deliver specific values from some lenders," said Don Kelly, the appraisal group's vice president for public affairs.

According to Mr. Kelly, some appraisers have been told by lenders, "If you can't come back with an appraisal that justifies this sales price, then we're not going to be able to use you."

The group wants "not only to call attention" to a "serious" problem but to "find a solution in the best interest of everybody," he said.

In 2001 the Appraisal Institute worked with a few lender groups to come up with a set of best practices, but the project fell by the wayside. However, the appraisal group is "intent on reinvigorating" the work this year, and this month it will co-host a conference call with the American Bankers Association and several federal regulators to discuss the problem, Mr. Kelly said.

Last year Rep. Jan Schakowsky, D-Ill., introduced an anti-predator bill that, among other things, would hold lenders accountable for appraisal values. Violators would be subject to criminal and civil penalties. The bill, which Mr. Kelly's group supports, has gone nowhere.

'Creating' Equity

As evidence that there is a problem, some appraisers cite foreclosure spikes in various parts of the country.

For example, foreclosures have more than doubled since 2001 in Gaston County, N.C., west of Charlotte. Bob Ipock, who runs the two-person appraisal outfit Ipock & Associates Inc. in Gastonia, said the closing of many textile mills in the county was only part of the cause.

Mr. Ipock, a 15-year appraisal veteran, said the local run-up in home prices over the past few years was hollow. "A lot of it was created" by demands on appraisers to put enough value on a home for the consumer to be able to get tens of thousands of dollars in extra cash by refinancing.

Brokers and loan officers will stop doing business with appraisers who get in the way of closing deals, he said.

"You get blacklisted," he said. "If we kill a deal, we've cost them thousands of dollars. If we're not able to 'hit the number,' we don't get any more work from them. They used to be more overt" about their wishes. "Now they're just not going to send you any more business."

Mr. Ipock said many mortgage brokers have stopped doing business with him in the past few years. His business has dropped 30% to 40% over the last six months, to about 15 to 20 appraisals a month.

He and other appraisers say loan officers and brokers subtly encourage inflated assessments by putting an "owner's estimate of value" on the appraisal order.

Consumers, and therefore the commissioned loan officers and brokers who pitch loans to them, "have unrealistic expectations," Mr. Ipock said. "Say someone has a house truly worth $100,000, they owe $90,000 on it, and they want to refi. They need $20,000 to pay off credit cards. They can't do the loan unless [the appraisal] comes in at $110,000 or $120,000."

Mortgage brokers have asked him to "create equity" where it does not exist, he said.

When local homeowners lost their jobs and flooded the market with houses for sale, the prices quickly dropped, he said. At the same time, other unemployed homeowners, whose houses had been overappraised, realized they owed more than their homes were worth, handed their lenders the keys, and compounded the price spiral.

"I would say locally our home prices have dropped 10% since two years ago," he said.

John De Nooy, the owner of De Nooy Appraisal Inc., in Knoxville, Iowa, 30 miles southeast of Des Moines, said the pressure from lenders intensified in 2000 and 2001 as debt-consolidation refis came into vogue.

"There were a lot of people doing refis. They had boats and campers and credit cards," Mr. De Nooy said. "That's when I think the lender was trying to get as much value out of the home to consolidate other debts. They just weren't being realistic."

Rich De Heer, who owns the Knoxville appraisal firm De Heer & Associates, said many questionable appraisals arise out of refis, where the appraiser "doesn't have a sales price to work off of."

They are also prevalent in rural communities where "you can go five or six blocks and be in a 20% higher real estate market," he said.

"A lot of these [overappraised] loans are being sold to secondary lenders," Mr. De Heer said, "and if they're selling these loans to somebody in Chicago, they don't know."

Client Pressure

Mr. De Nooy bought his residential business in April 2002 from Mr. De Heer, who still does commercial appraisals.

When Mr. De Heer used to appraise homes, he said he felt "client pressure," mostly from the Des Moines mortgage unit of Wells Fargo & Co., which was the top retail originator in the third quarter, and the largest over all, according to *National Mortgage News*.

Mr. De Heer had a long-standing relationship with Brenton Bank, a Des Moines lender that merged with Wells in 2001. He said the Benton loan officers he had dealt with in the past stayed at Wells, but when their compensation shifted to commissions from salaries, they became more aggressive in their demands for higher appraisals.

When his shop refused to play along, "we saw a real slowdown in orders, and they stopped altogether for two-month periods," and Wells was slow to pay for appraisals on loans that did not close, he said.

Mr. De Nooy, who does not appraise homes for Wells, said he did in mid-2003 a "field review" of a home in Knoxville. The noteholder had bought the loan from Wells, which had used a different firm for the original appraisal.

"We found that the comparables used in the original report were not comparable. The houses in the area were not as 'kept up' as the comparables," he said. "The first appraisal came in at $130,000. Our field review came in at $92,000. I sent it on, and I haven't heard anything since. Normally I don't hear anything."

Wells' Policy

Todd Bjorklund, Wells Fargo Home Mortgage's senior vice president of settlement services, working out of Edina, Minn., called the two Iowa

appraisers' comments "inconsistent with what we know to be true in experience and practice."

In an interview, Mr. Bjorklund said Wells thoroughly checks its thousands of approved appraisers. He and David Bialzak, Wells' division manager of credit risk management in West Des Moines, described the three-step process by which the company checks out appraisers' work.

Wells first reviews appraisals on all of its loans during the mortgage underwriting process. Mr. Bialzak said it then analyzes a "statistical sample" of the loans, as well as a sample of loans that are $1 million or bigger. Finally, both executives said, the corporate credit administration group at Wells' corporate headquarters in San Francisco conducts "periodic reviews" of appraisals.

The executives said they did not know the percentage of loans that get double- or triple-checked. Both said Wells' foreclosure rates were below the national average, but they would not release the figures.

In addition, Mr. Bjorklund said that in the "last few years" Wells has not had to repurchase any loans with inflated appraisals that have gone sour.

Making accurate appraisals is a discipline, and appraisers should not be swayed by anyone seeking a certain value, he said. "I would simply go back to the training and ethical piece of what that profession is asked to stand behind."

Natural Balance

Reports of overstated appraisals have not been limited to places like Gaston County or Knoxville.

"It's not just on rural property; it's nationwide," said Greg Hansen, the president of Fidelity Hansen Quality Inc., a San Diego unit of Fidelity National Financial Inc. that reviews appraisals for secondary loan buyers. "We look at appraisals all over the U.S. As a whole, 15% to 30% of them appear to be significantly overappraised, over 15% of what the property is really worth, including in metropolitan areas like New York and Los Angeles."

However, pressure from originators is probably not the only cause of inflated assessments, Mr. Hansen said. New appraisers with little expertise in their markets could also play a role, he said.

In his several decades as an appraiser, Mr. Hansen said he had never been "pressured" by brokers or lenders.

In his view, disagreements are inevitable between appraisers, who tend to be conservative, and originators, who tend to be more aggressive out of a desire to close deals. "It's like going to Vegas. A developer at the craps table is going to be much more aggressive in betting than an appraiser will be. It's that balance that everybody is working for."

Asking a broker to appraise a home for a certain value is "a natural level of pressure," Mr. Hansen said. "It's necessary, and if appraisers understand that and still give their real opinion of value, that's what they're supposed to do."

Appraisers are quick to say they are being pressured, and lenders and brokers are just as quick to deny it, but the truth is "really in the middle," he said. "If appraisers hold their ground, it creates this balance that there needs to be."

Adding Buffers

One way lenders can control the quality of appraisals is by centralizing orders, either with an outside firm or an in-house vendor management shop. Aside from the benefit of cost savings, this practice creates a buffer between the loan officer and the appraiser.

"Salespeople are always trying to get the deal done," but inflated appraisals are not a big problem right now, Angelo Mozilo, the chairman and chief executive of Countrywide Financial Corp., said in an interview.

Countrywide keeps close tabs on the appraisers it hires, including those registered with Landsafe Inc., its Plano, Tex. online settlement services unit, he said.

Using Landsafe helps Countrywide to maintain its integrity, Mr. Mozilo said. Because Landsafe is a Countrywide unit, "we control the appraiser; they work for us."

According to Landsafe's president, Steve Boland, the unit orders "the majority" of the appraisals on loans originated by Countrywide's retail channel.

In addition, Mr. Boland said in an interview, Countrywide has "a lot of controls in place to make sure we are comfortable with the collateral valuation."

However, many lenders that have vendor management shops do not mandate their use when ordering appraisals or other services.

"What We Need"

And, critics say, lenders have even less control when loans are arranged by mortgage brokers, who are free agents.

A senior manager at a national wholesale lender said it is "typical policy" for a broker to "send out appraisal requests" and tell appraisers "'This is the value we need. If the requested value is not there, do [an analysis of comparable sales] and then call us.' "

The executive, who requested anonymity, used to work at a large Los Angeles-area mortgage brokerage that had its own "in-house appraiser."

The appraiser "was just our pet," the executive said. "We had him in our pocket. He showed up every morning, we were one of his only clients, and if we got our values knocked, he would do a value review" - and the brokerage would get the value it wanted.

Lenders are "trying their best to catch these things," but with the volume of loans that were being brokered during the refi boom, they did not have the resources to thoroughly review appraisals on all the homes they finance, the executive said.

Recommendations from originators are encouraging appraisers to be more creative in their value assessments, the executive said. For instance, an appraiser who cannot find the "correct" home value by searching through comparative neighborhood sales data from the last two months will look for comparable sales in "surrounding neighborhoods."

A home that would have been worth only $530,000 when compared with other homes in its immediate neighborhood could be inflated to $600,000 or $610,000 by doing a wider search, the executive said. "Now the next person is going to see comps in the $600,000 to $610,000 range, and all of a sudden you have this whole new overinflated neighborhood."

Many lenders do very few field reviews, or secondary appraisals, on properties, the executive said. "They're turning a blind eye and trusting appraisers." But "if they go to sell" the loan, "they're going to be in trouble," because investors can force lenders to buy back loans that have inflated appraisals.

Not A Science

Chuck Reed, a senior vice president at ABN Amro Mortgage Group of Ann Arbor, Mich., the nation's largest wholesale lender, acknowledged that the problem of inflated appraisals exists.

However, it is limited to "less than 10% of the market," Mr. Reed said. "We have some good processes in place" to combat appraisal fraud.

The ABN Amro Holding NV unit tightly scrutinizes appraisers before it will work with them, and for the past year and a half it has run every single loan it originates through an automated appraisal checking system, he said.

If the system detects any abnormalities, ABN Amro Mortgage has a vendor management firm send a real estate agent to do a field review of the home, Mr. Reed said.

Amro also uses an automated valuation model to randomly review 10% of its loans, he said. It does field reviews on "less than 1%" of the loans it funds.

Instead of complaining, appraisers should do more "self-policing," Mr. Reed said. "Where are their ethics?"

He also disagreed with the popular argument among appraisers that they risk losing all their business by refusing to do inflated appraisals.

"In the refi boom there has been so much business, such huge backlogs," that the average appraiser "has had so much business they don't know what to do with it," he said. "You can't get business elsewhere? That's pushing the envelope."

Appraisals are "not a science," Mr. Reed said; they depend on local markets and a lot of detailed comparing of neighboring properties. It is not wrong for lenders to put on their appraisal requests what they think the house is worth, as it has become a custom, and appraisers even ask for it, he said.

Spiritual Issue

A.W. Pickel 3d, the president of the National Association of Mortgage Brokers, said brokers and loan officers should not be singled out. "Appraisers feel this pressure from realtors and consumers as well."

Inflated appraisals are a "short-term" fix, but "long term, they hurt everyone," he said - consumers lose equity, brokers lose clients, and lenders lose collateral value.

Brokers get a bad rap, because they are originating "close to 70%" of the nation's mortgages, Mr. Pickel said. "I don't think you're looking at a crisis. There are a few bad apples there, and they don't get better, they get rotten," but other, more conscientious originators "can turn ripe and become great companies."

His solution: Educate originators and form a national registry that would enable consumers to check up on their lenders, as they can with stockbrokers.

The mortgage brokers group has been backing mandatory broker licensing and education requirements for a couple of years, and has gotten requirements enacted in some states.

However, Mr. Pickel does not advocate regulations that would go further than licensing or education.

"I can't change someone's heart," he said. "I can educate people and show them by law that it's fraud, but it's a spiritual issue to change someone's heart. Added regulations" will not "stop the crooks."

Editor's note: This week's Pipeline column will run in Friday's paper.

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Appraisers Petition

Concerned Real Estate Appraisers from across America
Submit the attached petition (Which was posted on appraisersforum.com):

To: Mr. Ben Henson - Executive Director
Appraisal Subcommittee (ASC)
Federal Financial Institutions Examination Council
email: benh1@asc.gov

cc: Other state or federal agencies with authority in the following matter

"The ASC's mission is to ensure that real estate appraisers, who perform appraisals in real estate transactions that could expose the United States government to financial loss, are sufficiently trained and tested to assure competency and independent judgment according to uniform high professional standards and ethics." From the ASC website.

The concern of this petition has to do with our "independent judgment" in performing real estate appraisals. We, the undersigned, represent a large number of licensed and certified real estate appraisers in the United States, who seek your assistance in solving a problem facing us on a daily basis. Lenders (meaning any and all of the following: banks, savings and loans, mortgage brokers, credit unions and loan officers in general, not to mention real estate agents) have individuals within their ranks, who, as a normal course of business, apply pressure on appraisers to hit or exceed a predetermined value.

This pressure comes in many forms and includes the following:

- the withholding of business if we refuse to inflate values,
- the withholding of business if we refuse to guarantee a predetermined value,
- the withholding of business if we refuse to ignore deficiencies in the property,
- refusing to pay for an appraisal that does not give them what they want,
- black listing honest appraisers in order to use "rubber stamp" appraisers, etc.

We request that action be taken to hold the lenders responsible for this type of violation and provide for a penalty on any person or business who engages in the practice of pressuring appraisers to do dishonest appraisals that do not provide for independent judgment. We believe that this practice has adverse effects on our local and national economies and that the potential for great financial loss exists. We also believe that many individuals have been adversely affected by the purchase of homes which have been over-valued.

We thank you for your cooperation and assistance.

Sign this Petition Your name and any comments you wish to add will be added to these below

Oregon

John A. Kitzhaber, M.D., Governor

Appraiser Certification and Licensure Board
1860 Hawthorne Ave NE, Suite 200
Salem, OR 97303
Telephone (503) 485-2555
FAX (503) 485-2559
http://www.oregonaclb.org

March 26, 2004

Tewana Wilkerson
Office of Senator Wayne Allard
United States Senate
521 Dirksen Senate Office Building
Washington DC 20510-0606

Facsimile: 202-224-6471
US Mail

Re: Correction to the Official Record - Oversight Hearing Title XI

Dear Ms. Wilkerson,

On March 24, 2004 Mr. Charles Clark, Georgia Real Estate Commissioner, presented testimony at a hearing conducted by the Subcommittee on Housing and Transportation of the U.S. Senate Banking, Housing and Urban Affairs Committee.

In his testimony Mr. Clark named Oregon as a state that supports his proposal to eliminate the Appraisal Subcommittee. Mr. Clark incorrectly identified Oregon as a state that supports his proposal.

Please allow this letter to serve as a correction to the official record of the above referenced testimony. Oregon does *not* support the elimination of the Appraisal Subcommittee.

Respectfully Submitted,

Robert A. Keith, Administrator
Oregon Appraiser Certification and Licensure Board

Cc: Charles Clark, Georgia Real Estate Appraisers Board
David Bunton, The Appraisal Foundation
Ben Henson, Appraisal Subcommittee

STATE OF COLORADO

BOARD OF REAL ESTATE APPRAISERS
Stewart A. Leach, Program Administrator

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Department of Regulatory Agencies
Richard F. O'Donnell
Executive Director

Division of Real Estate
Debbie Campagnola, Director
Jeff Foster, Deputy Director

Bill Owens
Governor

March 18, 2004

The Honorable Wayne Allard
521 Dirksen Senate Office Building
Washington, DC 20510

Re: Subcommittee hearing on real estate appraiser regulation

Dear Senator Allard and Members of the Subcommittee:

The Colorado Board of Real Estate Appraisers has been informed of your Housing and Transportation Subcommittee hearing on the status of real estate appraiser regulation. We wish to offer our comments and perspectives. Please make this letter a part of the proceedings of the Subcommittee.

Brief history:

Colorado adopted legislation in 1990 to implement the requirements of Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"). The first licenses were issued in July 2001. The Board now has 2998 appraisers eligible for federally related transactions.

The Appraisal Foundation, named in FIRREA as the source of licensing requirements and professional standards, initially set licensing criteria quite low. The plain intent was to set minimal education, examination and experience requirements that could be met by most existing practitioners, in order to avoid an immediate shortage of licensees eligible for federally related transactions. Minor changes to the requirements were made in the early 1990's.

Time has shown the present requirements are not sufficient to prepare appraisers for the demands of practice in the increasingly complex world of modern real estate. The Appraisal Foundation recently promulgated much higher requirements, to go into effect January 1, 2008. The Colorado Board participated in the development of these new requirements, and believes them to be appropriate. We do wish the changes had been developed and implemented in a series of smaller hurdles, instead of the coming pole vault. State regulators, education providers and others are preparing for the change.

What's going well:

The states and other jurisdictions have implemented licensing programs, some more effectively than others. The FFIEC Appraisal Subcommittee ("ASC") does an effective job of monitoring and assisting the states as they carry out the intent of FIRREA. The Colorado Board does have concerns

about some ASC members apparent lack of respect for due process for licensees who have failed to meet continuing education requirements. The states organized the Association of Appraiser Regulatory Officials, which has been highly successful in promoting cooperation among licensing jurisdictions, federal agencies, professional associations, related industries and educators.

Problem areas:

The number one problem impacting state regulation of real estate appraisers is lack of adequate funding. As an example, the budget crisis in Colorado led to a hiring freeze that left our only complaint investigator position vacant for over six months. Despite best efforts, we have a serious backlog of complaints waiting for investigation. Time to review licensing applications has gone from 10-12 days to well over 30 days. Similar conditions exist in most of the states. If Congress wants effective appraiser regulation to protect the public and federal interests, the funding problem must be solved.

Two decades ago, a residential borrower went to their local bank, savings and loan or credit union to apply for a mortgage. Now, the application process has been outsourced to mortgage brokers who are wholly commission compensated. These mortgage brokers put unconscionable pressure on appraisers to "make my deal"- to pump up the value conclusion. This pressure is especially acute in the refinance market. Public harm and injury to federal financial interests is increasing.

The various federal financial regulators, secondary markets and guaranty agencies do their best, but their reach stops at the organizations that fund or guaranty the loans originated by mortgage brokers. There needs to be greater depth of control in the residential mortgage process. We also see a need for the several federal housing agencies- VA, FHA, Fannie Mae, Freddie Mac and the like- to do more front-end quality control of the loans they purchase or guaranty. Reviewing appraisals and other loan documentation after default and foreclosure does not protect public or federal interests.

The Colorado Board has increasing concerns with the various "seller assisted down payment" programs, where the seller makes a "contribution" to a "charitable organization" that then makes a "gift" to the purchaser to use for down payment and closing costs. These transactions are a *quid pro quo*- no "contribution" equals no "gift". Our research shows many properties sold through these programs are financed for more than their market value. Most of these transactions involve first time homebuyers and FHA guaranteed loans.

Thank you for considering these remarks.

Sincerely yours,

for the COLORADO BOARD OF REAL ESTATE APPRAISERS

Stewart A. Leach
Program Administrator

STATEMENT OF THE NATIONAL ASSOCIATION OF REALTORS®

MARCH 24, 2004

Mr. Chairman, Members of the Subcommittee, the National Association of Realtors® (NAR) appreciates the opportunity to submit written testimony regarding the Real Estate Appraisal Industry and Title XI of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA). NAR is the Nation's largest professional trade association with almost a million members and is comprised of over 1,500 realtor associations and boards at the State and local levels. NAR membership includes brokers, salespeople, property managers, appraisers, and counselors, as well as others engaged in every aspect of the real estate industry.

NAR commends the Subcommittee for its leadership in recognizing that the real estate industry has changed, and also in asserting your proper role to examine the effectiveness of the current Federal and State regulatory structure as set forth in Title XI of FIRREA. NAR also applauds the Subcommittee for highlighting the General Accounting Office's (GAO) report on enhancing oversight of the real estate appraisal industry. The GAO report points out that Federal, State, and private entities face impediments in carrying out essential activities called for in Title XI of FIRREA. In addition to impediments, agency regulatory officials, mortgage industry representatives, the Department of Housing and Urban Development and Government Sponsored Enterprises such as Fannie Mae and Freddie Mac all raised concerns about the regulatory structure created by Title XI. NAR believes that the current regulatory structure is overly complex, inconsistent from State-to-State and in need of thorough review and examination by Congress.

Title XI of FIRREA

Lack of Consistent Enforcement

Title XI of FIRREA was enacted to protect Federal financial and public policy interests in real estate related transactions by requiring that real estate appraisals be performed by individuals with demonstrated competency. Since FIRREA was passed 15 years ago, and because it mandated State licensing under Federal standards, the regulatory structure for appraisers has evolved into a unique and complex system. It involves licensing boards in the various States, qualification criteria and uniform standards set by the Appraisal Foundation, and Federal oversight by the Appraisal Subcommittee of the Federal Financial Institutions Examinations Council. State licensing boards license, certify and provide oversight and enforcement of nationally recognized standards (the Uniform Standards of Professional Appraisal Practice) and State laws.

Since Title XI was enacted, it has been difficult to achieve necessary consistency among the States for enforcement of both standards and certification requirements. With a patchwork of State laws and ineffective Federal oversight allowing for only "minimum" qualifications criteria for licensing and certification in some cases, States and the Federal oversight bodies have too often not carried out their specific intended responsibility to enforce the standards as required by the Federal law. Too often, complaints against real estate appraisers in some States are not reviewed by State appraiser boards, leading to a lack of disciplinary action against poorly performing appraisers. Other boards have been known to spend inordinate time and research and collect fines for inconsequential offenses, leaving little time for enforcement of major issues.

The lack of consistent enforcement among the States is due in part to the fact that many States do not adequately fund enforcement and licensing. As a result, certification boards are forced to choose the cases that are investigated based on the nature of the violation, as opposed to investigating each complaint thoroughly. Additionally, there is no consistent requirement among the States that either appraisers or lenders report erroneous appraisals to the State enforcement board. Also, some States see the requirement to certify licensing as an unfunded Federal mandate, and with many of them facing budget restraints it is not difficult to see why there is not uniform enforcement.

Even though adequate funding of the licensing, certification, investigation, and disciplinary activities may be a problem in some States, it is by no means universal or pervasive. States actually do license and certify appraisers and evaluate, approve, and disapprove prelicensing educational offerings. States do evaluate, approve, and disapprove continuing education course offerings and require regular continuing education of their licensees. States receive complaints, investigate, and prosecute appraisers for violations of their license law and the Uniform Standards of Professional Appraisal Practice (USPAP). However, one of the major problems is that States rarely receive complaints from the federally regulated lenders, HUD, VA,

Fannie Mae, and Freddie Mac. These entities too often fail to inform States of poor appraisals, poor practitioners, or fail to file complaints with the appropriate State-licensing agency or if they do so, do it in an incomplete and lackadaisical manner.

Lack of Qualified Appraisers

Many State appraisal boards fail to resolve complaints against real estate appraisers in an expeditious manner. Whether through a lack of resources or a lack of will by those charged with providing oversight, the current system allows some unscrupulous and unqualified appraisers to continue practicing with little or no recourse for their actions.

One of the fundamental goals of Title XI was to raise the professionalism of appraisers involved in federally related transactions, however, this has not been met. Having provided for only "minimum" qualification requirements, the implementation of FIRREA has failed to offer incentives for appraisers to seek additional training, education, and experience. We believe the public would be better served by a system that encourages appraisers to excel through appropriate professional development because many appraisers see acquiring a license as the be-all and end-all of becoming an appraiser. NAR supports a licensed or certified appraisal for all federally related transactions. NAR believes that relying on appraisals more often will lead to better loan underwriting. NAR believes that appraisals performed by certified and licensed practitioners with higher than minimal qualifications will help protect consumers from unscrupulous lenders and inflated transactions.

Lack of Purpose and Direction for the Appraisal Foundation, Appraisal Standards Board, Appraisal Qualifications Board, and Appraisal Subcommittee

NAR is concerned about the direction and purpose of the Appraisal Foundation, the Foundation's Appraisal Standards Board (ASB), and the Foundation's Appraiser Qualifications Board (AQB). NAR questions the propriety of a private organization (Appraisal Foundation) promulgating standards for appraisals and qualifications of appraisers, which must then be adopted and enforced by State regulatory agencies. These standards and criteria have the effect of law but they have been adopted completely outside the State legislative process. Appointed individuals without any type of Government control or oversight have the power to promulgate these standards. Even though the standards and criteria are issued for public comment, they are nonetheless discussed, debated, decided, and mandated by independent and autonomous Boards of the Appraisal Foundation in nonpublic meetings. This is in direct contradiction to some State laws.

NAR also questions the lack of responsiveness and accountability from the Appraisal Foundation, its ASB, and its AQB to their professional association sponsors. There is a significant amount of concentrated power given to a relatively small number of individuals where the sponsoring organizations have no means of appointing or providing oversight. For example, NAR has tried for several years to limit the USPAP to "Appraisal Practice" by asking that Standards 4 and 5 be removed from the document because we believe, along with other groups, that Title XI pertains to appraisals, not consulting assignments. We contend that the mandate to the States in Title XI was to license, certify, and regulate appraisers, not counselors.

In some States, the Appraisal Foundation, the ASB, and the AQB have exceeded their authority and have, in effect, acted as regulatory bodies over the State regulatory agencies. For example, the AQB has previously restricted the licensing authority of some States. They have disapproved a number of State-approved prelicensing and continuing education courses because of minor technical differences and have imposed their own arbitrary criteria.

The AQB has adopted a number of arbitrary requirements, which could be construed as conflicts of interest. For example, the national USPAP course mandated by the AQB requires either AQB approval or use of their course and examination with royalty paid to the AQB. The national USPAP update course and examination has a similar approval structure. Also, the AQB requires all USPAP instructors to meet their standards and only instructors taking an Instructor Certification Course can meet the standards. The only approved Instructor Certification Course is presented by the ASB and taught by ASB members.

The purpose of the Appraisal Subcommittee is to provide control and oversight of the Appraisal Foundation, the ASB and AQB, and to protect the public, appraisers, and instructors from these conflicts. However, the Appraisal Subcommittee often remains silent and thus conveys the impression that they are working in concert with the Appraisal Foundation and the members of its ASB and AQB. NAR recommends that an appeal process to an independent third party be established and courses and instructors be approved by either the State Licensing Board or the AQB.

NAR believes that there is a lack of consistent and effective oversight of State appraisal boards by the Appraisal Subcommittee. Oversight of all State regulatory boards is vested in the Appraisal Subcommittee; however, the Appraisal Subcommittee is made up of representatives of the lending and banking industry—designees of the heads of the Federal financial institutions regulatory agencies. In our opinion, the current oversight of the Appraisal regulatory structure is more vested toward the lending industry. The problem is that these regulatory agencies are the ones that regularly propose and pass rules to increase the de minimus level. By increasing the de minimus level, they reduce the consumer protections that Title XI of FIRREA was intended to provide by requiring appraisals for all federally related transactions. As the de minimus level is increased it negates the need for an appraisal thus denying protections to the consumer.

Appraisals and the De Minimus Level

Over time, most residential real estate transactions have been exempt from obtaining an appraisal because the de minimus level, in which a certified or licensed appraisal would be required, has been raised to $250,000. NAR has had long standing policy that the de minimus level for residential property should not exceed $100,000. There are a large number of transactions that could avoid the appraisal process altogether because the median sales price in many major markets and smaller markets is below $250,000.

NAR recognizes that there are cases when an appraisal for a mortgage loan transaction should not be a requirement, but relying solely on the dollar amount of the transaction as the determinant is a poor measure. There are other factors such as loan-to-value, predominant value in the region, qualifications of the borrower, strength of the real estate market and its trend that should be considered as well.

Recognizing that the de minimus level in all likelihood will not be lowered back to $100,000 for residential loans, NAR believes that lenders should be required to inform a borrower of the methods used to value a property to determine the amount of the mortgage loan, and that borrowers should have the right to be provided with a copy of each value estimate or value opinion obtained. Many buyers, particularly first-time buyers, are not aware of their options and rights. They do not fully understand the purpose of the appraisal or value estimate and may not be taking full advantage of the safety, security, and utility of an independent, third party opinion of value. NAR firmly believes a full appraisal report, prepared by a State-certified or licensed appraiser, may be useful to the buyer in assuring them of the validity of the price paid for the property and securing the proper amount of insurance.

Further, lenders often obtain multiple estimates or opinions of the value of the collateral. In the event that more than one estimate is obtained on behalf of the borrower, NAR believes that the consumer should be provided with all of the value estimates or opinions of value. In this way, the purchaser can be assured that the value estimate supports the price of the property.

Lender Pressure

There are some participants in the mortgage process that pressure appraisers in order to ensure that their estimates of the fair market value of collateral property are sufficient to make predetermined loan amounts. Increasingly, there is evidence that the use of such pressure is widespread in the appraisal field. These pressures are beginning to erode the independent judgment of appraisers, and are contributing to the ability of unscrupulous individuals to engage in improper loan practices, including property flipping and predatory lending schemes. While the most immediate victims of these practices are the elderly, lower-income families, and other vulnerable consumers, they also damage mainstream lenders and Federal housing assistance programs.

Conclusion

NAR believes that the oversight of the appraisal regulatory structure should be geared toward the interests of consumers and the protections the consumer should expect from an independently developed, unbiased, objective third party opinion of value of the real property offered as security for a loan. The Uniform Standards of Professional Appraisal Practice (USPAP) were originally developed by professional appraisal organizations to ensure public trust in the appraisal profession. We believe the standards should concentrate on their original purpose, which is to ensure trust in the appraisal practice. Finally, the failure to report faulty appraisal reports and deficient appraisers to the appropriate State regulatory boards continues to be a serious problem.

NAR appreciates the opportunity to share its views and observations and we stand ready to work with the Subcommittee to improve effectiveness of the current Federal and State regulatory structure as set forth in Title XI of FIRREA.