



FEATURE

Regulating Real Estate Appraisers

First Came FIRREA, then Dodd-Frank.
What's the Next Wave in Oversight for
Real Estate Appraisers?

By Greg Stephens, SRA





The degree of oversight and regulation affecting the appraisal industry today got its roots as a result of the Savings and Loan (S&L) crisis of the 1980s.

As a result of that crisis, Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), creating for the first time a federal oversight system regulating valuations conducted for federally related mortgage lending transactions within Title XI of the Act. These new rules continued to morph into the regulations we are doing business under today, such as The Dodd-Frank Wall Street Reform and Consumer Protection Act, and the regulatory environment will continue to be a hot topic for appraisers in 2015 and beyond.

Uncharted Course: The Appraisal Industry Prior 1989

Prior to the passage of FIRREA (which at the time was referred to as Federal Interference Regarding Real Estate Appraisals) the appraisal community was a self-regulated industry where membership in national appraisal organizations and their respective designations represented an appraiser's level of experience and expertise. The system of accountability resided in the by-laws of the various appraisal organizations governing the ethical and competent activities of the designated members and those pursuing designations enabling the organizations to self-discipline and mentor through a peer review process, those involved with the organizations, including revoking if necessary those with the designations.

Unfortunately approximately only 30 percent of practicing appraisers in 1989 belonged to a national appraisal organization. The other 70 percent had no affiliation with a professional appraisal organization

and as such were accountable to no one other than their clients, and the only consequence for unethical or incompetent behavior was possibly the loss of business.

The paradigm shift spurred by the S&L crisis relates to the creation of The Appraisal Foundation, the Uniform Standards of Professional Appraisal Practice (USPAP), the Appraisal Subcommittee (ASC) that oversees the activities of The Appraisal Foundation, and the state appraiser regulatory agencies in the post-FIRREA world of valuations for federally related transactions.

These entities were created in response to appraisers being blamed in large part for the savings and loan failures in the 1980s.

Title XI of FIRREA required the establishment of the state appraiser regulatory agencies to oversee the licensing and certification of appraisers in all 55 states and jurisdictions.

The Appraisal Foundation Appraiser Qualifications Board became the entity establishing the minimum education and experience requirements for appraisers to qualify for state appraiser licensure or certification. The Appraisal Foundation Appraisal Standards Board became the entity establishing and administering the minimum standards of competency and ethical behavior appraisers must adhere to in order to retain their state licensure and certification.

In the 1990s and early 2000s that all seemed to be working. Appraisers were getting licensed and certified in the various states and the state appraiser regulatory agencies were taking action against the licensed and certified appraisers who were violating USPAP or otherwise egregious behaviors putting the public at risk.

And then along came the mortgage market meltdown of 2008.

A New Era Begins: Introduction of Dodd- Frank

In response to the meltdown of 2008, in 2010, the U.S. Congress passed a new set of regulations known as the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Signed into law by President Obama in July 2010, it has been referred to as the most comprehensive financial regulatory reform measures taken since the Great Depression. The enrolled bill is more than 2,200 pages in length and has a word count of 383,013. It comprises sixteen titles, requires 243 new rules, created 12 new regulatory agencies, and will take more than five years to implement at a cost in excess of \$30 billion.

As comprehensive as it is, the Dodd-Frank Act introduced minimal changes in the oversight of real property valuations.

Real property valuation oversight is contained in Title XIV, the Mortgage Reform and Anti-Predatory Lending Act, which among others, created a new bureau called The Consumer Financial Protection Bureau (CFPB) tasked with the administration of the new laws and regulations.

Subtitle F-Appraisal Activities contains revisions to TILA (Truth in Lending Act) relating to Higher Risk Mortgages requiring creditors to obtain an on-site, full interior appraisal by a certified or licensed appraiser and established requirements for a second appraisal for rapid-resale transactions.

TILA amendments also expanded appraiser independence guidelines and payment of Reasonable and Customary Fees paid to appraisers.

Although the Federal Reserve Board published the Interim Final Rules relating to Reasonable and Customary Fees in October 2010, the fee issue remains one of the most widely discussed and debated issues within the valuation community.

Other regulatory changes in the Act and in the subsequent Final Rules published by the Agencies worth mention include conflict of interest and appraiser independence.

In response to the proliferation of appraisal management companies following implementation of the Home Valuation Code of Conduct and concerns expressed by industry participants, Congress also included AMC's regulations, specific prohibition language relating to appraiser independence, and the prohibition to have either a direct or indirect interest, financial or otherwise, in the property or transaction involving the appraisal.

Another significant TILA amendment was the mandatory reporting requirement for any mortgage lender, mortgage broker, mortgage banker, real estate broker, appraisal management company, employee of an appraisal management company, or any other person involved in a real estate transaction involving an appraisal in connection with a consumer credit transaction secured by the principle dwelling of a consumer who has a reasonable basis to believe an appraiser is failing to comply with USPAP, is violating applicable laws, or is otherwise engaging in unethical or unprofessional conduct. If such unprofessional conduct is observed by any of those named, they are required to refer the matter to the applicable state appraiser certifying and licensing agency.

FIRREA Title XI was also amended in the Dodd-Frank Act, the most significant changes since enactment in 1989, which included modification to 13 of the original 25 sections and the addition of three new sections.

One of the new sections (1124), established minimum requirements for states to establish registration requirements for appraisal management companies. Per Section 1124, the states are required to implement laws requiring AMC's to:

- Register with and be subject to



supervision by state appraiser regulatory agencies;

- Verify that only licensed and certified appraisers are used for federally related transactions;
- Require that appraisals comply with USPAP; and
- Require that appraisals are conducted independently and otherwise adhere to the TILA appraisal independence standards.

Section 1124 of FIRREA went into effect on January 21, 2013.

To date 38 states have enacted some type of AMC registration legislation.

Another game changer is found in Section 1126 containing a general prohibition relating to the use of BPOs as the primary basis to determine the value of property to be secured for mortgage origination in conjunction with the purchase of a consumer's principle dwelling.

The Interagency Appraisal and Evaluation Guidelines were published by the federal regulators in December 2010, providing clarification to compliance requirements relating to appraisals and evaluations, when an appraisal is required, when an evaluation may be used in lieu of an appraisal, the content of an evaluation which now includes knowledge of the property condition and a statement of most probable market value.

One of the more significant clarifications by the agencies is found in the Chapter XVI (Third Party Arrangements) where the agencies made it crystal clear that a lender outsourcing any part of the collateral valuation function should exercise due diligence in the selection of a third party and that the institution should be able to demonstrate that its policies and procedures establish effective internal controls to monitor and periodically assess the collateral valuation functions performed by a third party.

The Guidelines also state that an institution is responsible for ensuring that a third party

selects an appraiser or person to perform an evaluation who is competent and independent, has the requisite experience and training for the assignment, and thorough knowledge of the subject property's market.

GSE Involvement: The Unofficial Regulators

Ironically, although not considered law or regulation, the guidelines published by the GSEs, and most notably Fannie Mae, have a major impact on the acceptability of appraisal reports generated for mortgage

According to individuals at Fannie Mae, so far over 14 million appraisal reports have been transmitted through the data portal, allowing the analysts to slice and dice the data. Using advanced technology, the analysts at Fannie Mae have been able to develop a comprehensive risk management tool, and on January 26, 2015, Fannie Mae released the Collateral Underwriter making it available to Fannie Mae's Corresponding Lenders.

It is the opinion of many in the industry that Collateral Underwriter is the next paradigm in the industry. Lenders

appraisal including data integrity, comparable selection, the adjustments, and reconciliation.

The communications from the lenders and their review staff back to the appraisers are not about whether they are in compliance with a federal or state law, or in compliance with USPAP, but rather whether the data in the appraisal report is consistent or inconsistent with Fannie Mae's proprietary database information and consistent or inconsistent with the way in which the appraiser's peers used and analyzed the same data. It is about degree of risk, not compliance with laws and regulation, yet CU will have more impact upon the development of appraisals than any other law or regulation since creation of appraiser state regulatory agencies.

A Look Ahead: The Next Wave of Appraisal Regulations

While the appraisal industry has come a long way from its Wild West roots of little oversight, this does not mean that further regulations won't continue to shape the industry. The regulators are currently finalizing the Rule-making pertaining to appraisal management companies, which was a requirement included in the Dodd-Frank Act.

In addition, the Appraisal Standards Board published the most recent version of USPAP in January 2014, with the next revision to become effective January 1, 2016. Additionally, the Appraiser Qualifications Board implemented a college degree requirement for certified appraisers effective January 1, 2015 and moved back the requirement for background checks to January 1, 2017. **M**

While the appraisal industry has come a long way from its Wild West roots of little oversight, this does not mean that further regulations won't continue to shape the industry.

lending and at the present time have as much impact on the development of appraisals as the Uniform Standards and state regulations.

In 2009, Fannie Mae published the first set of Unacceptable Appraisal Practices, which have since been modified, expanded, and included in the current Fannie Mae Selling Guide available on their website.

In September 2011, Fannie Mae implemented the Uniform Collateral Data Portal and Uniform Appraisal Dataset (UAD) intending to standardize data contained in appraisal reports electronically submitted through their data portal.

now have access to massive amounts of data and analytics to assess risk in the valuation reports being electronically submitted through the data portals. The data, analysis and conclusions of an appraiser are being captured in real time and compared to the selection and analysis, of that same data used by their peers through the application of proprietary analytical models to analyze key components of the



GREG STEPHENS, SRA is a recognized subject matter expert in appraisal regulations and standards whose 37 years in the industry include owning a regional appraisal firm in Northern California, national lender QC/compliance and most recently as Chief Appraiser, SVP Compliance for Metro-West Appraisal Company LLC.