APPRAISAL TODAY

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Appraisal Today newsletter 25th Anniversary!!\ Changes over the past 25 years. What a wild ride it has been!!

The first issue of this monthly newsletter, then called Appraisal Management and Marketing was published June 1, 1992. In June 2012 I published a 20th Anniversary 17-page newsletter going over the changes since 1992. This article focuses on changes since 2012, with summaries of previous changes.

There is a copy of the June 2012 newsletter on the paid subscriber page if you want much more detail on changes up to 2012. Since 2012, the main changes have been UAD and CU, discussed below.

The most significant changes for appraisers: FIRREA licensing, Dodd-Frank were responses to lender problems. FIRREA was a reaction to poor commercial lending, but affected both residential and commercial appraisers. Dodd-Frank and Fannie's UAD and Collateral Underwriter were reactions to residential lending problems and significantly affected residential appraisers.

Lots of significant changes since 1992, including
• Appraisal licensing
• USPAP adopted and changes every two years
• Two appraisal recessions (early 1990s and 2008+)
• Shift from lender originations to mortgage brokers, then to AMCs (since licensing in 1992-1993)

Since 2012, the most significant change is Collateral Underwriter, which had resulted in changes in appraisal reporting, increasing scope creep, and database use by Fannie to analyze appraisals.

Another recent substantial change is the shift to fees based on supply and demand. Starting a few years ago, with the large volume increases, fees went up. Many AMCs increased fees to get appraisers to accept their orders. Some direct lenders had a few changes in fees.

When volume starts declining, as it already has, fees will go down again. VA significantly increased their fees. VA fees don't change quickly.

Whether or not they will g down when volume drops is not yet known.

HVCC/Dodd Frank summary of changes and time line

AMCs took over appraisal ordering and managing. This significantly affected appraisal fees and relationships with clients. A very negative result for some AMCs was their treating appraisers as all the same, not as professionals.
• 3/3/08 Fannie/Cuomo agreement signed
• 3/09 New Fannie guidelines, implementing HVCC
• 5/1/09 HVCC effective
• 7/10 HVCC expires, superceded by Fannie guidelines
• 7/1/10 Dodd Frank Wall Street Reform and Consumer Protection Act
• 11/10 Interim Final Rule issued - includes how to set customary and reasonable fees
• 4/1/11 Final Rule effective for appraisal fees and independence, supercedes HVCC

Time line: Pre-HVCC - appraiser complaints about pressure by mortgage brokers time line

Appraisers protested. Mortgage brokers gone after 2008 Mortgage Meltdown. Appraisers got AMCs.
• 2001 - Appraisers Petition protesting pressure has over 11,000 names and is closed to further names - already had enough.
• 2001-2009 - many appraisers, appraisal associations, and others complained about the pressure.

• Early 2007 - Florida appraiser Pamela Crowley states on her web site, wwww.mortgagefraudwatch.com that eAppraiseIT had been opening appraisal PDFs. eAppraiseIT filed a lawsuit which it later dropped. Lots of national news on this.
• May 2007 - New York attorney General Andrew Cuomo issued a subpoena to eAppraiseIT in his investigation of whether mortgage brokers pressured appraisers to inflate property values. eAppraiseIT values up to 15,000 homes a year in New York, per the president, Anthony Merlo Jr.
• 3/3/08 Fannie/Cuomo agreement signed

Time line: Fannie forms

As you can see below, there were few changes in Fannie appraisal forms over the years.
• Mid-1970s - Fannie Mae standard form, called the "Green Hornet" because of its color on the side bars.
• 1987 The new URAR was effective 4/1/87
• 1992 - Revised URAR (and other forms) implemented.
• 2005 Revised URAR (and other forms). Changed length and formatting with more blank space available for comments and optional Cost and Income Approach sections. New 2055 (driveby) form.
• 4/1/09 1004MC Addendum t URAR required. Response to dramatic increase in foreclosures. Appraisers no longer lost clients because they made market conditions adjustments.

Appraiser licensing summary of changes

Licensing dramatically changed appraising, especially for residential lending. Appraisers were subject to a national USPAP that regularly changed, state regulators, increasing requirements for licensing, etc.

• 8/89 - FIRREA/Title XI requires state appraiser licensing
• 1991- AQB establishes initial requirements for certified appraisers
• 1998 - Increased education and experience.
• 2008 - Increased education and experience plus added college level course requirements
• 2015 - Increased education and experience. 4 year degree requirement for certified appraisers proposed
• 2017 - changes proposed because of perceived appraiser shortage. Alternate path for upgrading from licensed to certified (CLEP, etc.). Requiring a college degree, especially for certified residential appraisers is still controversial.

FHA summary of changes
• 12/2/94 new regulations - new fee appraiser panel, open FHA to all licensed and certified appraisers with training
• 1/1/96 FHA Fee Panel eliminated (not open to all licensed appraisers and could be hard to get on the panel)
• 1/30/99 - passing FHA exam required
• 2005 - Valuation Conditions (VC) form eliminated
• 2/1/08 - exam eliminated
• 10/1/09 FHA requires state certification. Another response to Mortgage Meltdown.
• 1/1/10 FHA does not allow mortgage broker originations

UAD, AQM and Collateral Underwriter Time Line

Data collection (UAD) for Fannie use in Fannie's appraisal analysis - adjustments, variations, etc. for data standardization. Fannie's response to the Great Recession and value declines.
• 9/11 - UAD data collection begins. Previously had only done post-funding reviews of appraisals.
• 7/12 - UAD testing starts. Lenders required to submit UAD data from appraisals. Use of UAD data to analyze appraisals focusing on data completeness and formatting.
• 2013 Fannie starts pre-funding reviewing of all appraisals.
• Late 2013 - Final UAD implementation date.
• Mid 2013 - Fannie starts setting up AQM (Appraiser Quality Management) "Do Not Use" list. As of 1/14 there were no appraisers on the list. Fannie started sending warning letters to appraisers. There is no data on how many appraisers are on the monthly AQM lists. There are two lists: appraisals are no longer accepted by Fannie appraisers or reviews are required on 100% of the appraiser's appraisals
• January 26, 2015 Collateral Underwriter, including Risk Scores, is released. Only 2.5 years ago!

UAD - late 2013 implementation

The objective of the UAD is standardized appraisal form data to make "big data" available for Fannie appraisal analysis, including adjustments.

Data is the "Holy Grail" of real estate analysis, where there are standardized choices for some of the data in Fannie appraisal forms.

Over 20-25 years ago, appraisers met to figure out the appropriate choices for Design, View, etc. It was very, very difficult.

Appraisers had to learn how to use sometimes ambiguous C and Q ratings. Many were very upset about the infamous "other appraisers" who could not accurately measure and calculate GLA, comparison with public records, etc.

Fannie warning messages declined between late 2012 and Quarter 1, 2017

Appraisers were notified when there were "problems" with their appraisals - data and analysis.

Adjustments and comparables messages have increased, but number of messages has declined. The decline in number of messages is reasonable as it has taken appraisers awhile to figure out the UAD and CU requirements. Plus, underwriters were confused about how messages were given to appraisers and too many were passed through by lender underwriters.

The increase in adjustments and comp messages is probably because Fannie has been focusing on these issues recently. Policy compliance and property eligibility messages focusing on data completeness and formatting have declined as more people got used to UAD requirements.

Messages for adjustments and comparables increased as Fannie started emphasizing these. Data discrepancy compared the subject's data to other information sources including other appraisals.

Percent of message types:

	Late 2012	Q1 2017
• Data reasonableness	48%	n/a (UAD) (Mostly UAD errors)
• Policy compliance	9%	n/a (UAD)
• Property eligibility	8%	n/a (UAD)
• Data Discrepancy (comparison with other appraisers)	n/a	46%
• Adjustments	29%	43%
• Comparables	6%	10%
• Reconciliation	1%	n/a

Number of messages has declined

Late 2012: Averaged 3-4 messages per report

Quarter 1, 2017: 60% have none or one messages. 80% had 2 or fewer messages.

Collateral Underwriter started 1/26/16

Fannie started using UAD data for primarily analyzing appraiser adjustments and secondarily comparable selection analysis.

CU dramatically changed appraisal adjustment analysis and requirements. I never received any training in any of my appraisal classes except for "paired sales", which is very elusive and not always reliable. It also made residential form appraising much, much more difficult and time consuming.

I quit making any adjustments, except market conditions and critical factors such as view, over 2 years ago as my state regulator wanted to see support. Very difficult to do as I don't do any work in larger home tracts.

What is the purpose of CU for Fannie?

In the past, Fannie did not do pre-funding reviews of appraisals. They only did post-funding reviews of about 10% of the appraisals they received. After the Mortgage Meltdown it was obvious changes were needed.

Per Fannie, "The purpose of Collateral Underwriter is to identify appraisals with heightened risk of property eligibility or policy compliance violations, overvaluation, and
appraisal quality issues."

"CU provides lenders with additional transparency and certainty by providing them access to the same appraisal data and analytics used in Fannie Mae's quality control framework."

"In summary, our objective is to distribute CU to support more proactive management of appraisal quality by empowering lenders to address potential appraisal issues prior to loan delivery."

CU and Comparable analysis

Per Fannie, "Collateral Underwriter's comp selection model is one feature that makes it unique. CU takes into account physical similarity, time, and distance when analyzing the overall relevance of comp transactions. The significance of each of these factors may vary from market to market and may change over time. "

"CU does not assign a fixed weight for each of these factors, but instead uses advanced statistical analysis to treat each appraisal and each market differently."

There are many more messages about adjustments than comparable selection. I assume that means that appraisers, per CU software, are better at selecting comps. That makes sense, as this has always been an important part of appraising.

Unfortunately, adjustments was never that important.

Appraiser licensing, the good and the bad

I started appraising in the late 1970s and started my appraisal business in 1986, before licensing. Most appraisers were taught how to appraise, and appraisal ethics by their employer: lender, assessor, etc. Few appraisers were trained by other appraisers.

We all knew what you were supposed to do: give an unbiased, honest opinion of value and tell the truth about what you observed about the subject and its place in the market.

Professional associations had standards, but they only applied to members. (That was the basis for the USPAP.)

Appraising was a profession, not an "industry". Appraisers were selected on the basis of their experience and professional qualifications. There were a few "I will give you the number" appraisers, but there were not very many. Lenders had fee panels and most appraisers knew their lender clients personally.

Many residential appraisers belonged to professional appraisal associations, which provided an excellent way to meet other appraisers and lender chief appraisers.

Membership in these associations was important for appraisers, whether staff or fee. Having a designation was very important. Those associations, for residential appraisers, have lost many members as state licensing replaced association membership as the way to get a job or having an appraisal business.

The associations opted out of basic appraisal education and focused on getting more designated members, losing an entire generation of appraisers.

After licensing, over time, the primary criteria for selecting an appraiser, particularly for lending, became a license. When AMCs took over, this accelerated as lenders did not choose their appraisers and did not know them. All appraisers were seen as the same.

Positive effects of licensing - summary

1. Appraisers could be disciplined.
2. All licensed appraisers had the same standards - USPAP
3. Defined path to "becoming" a professional appraiser
4. Licensed appraisers could get MLS access.

Negative effects of licensing - summary

1. The primary criteria for appraisal selection is having a license for many clients, especially for residential appraisers.
2. State appraisal board regulations vary widely around the country.
3. Costs of keeping a license.

4. If a license is given up, very difficult to get back in many states.

Increases to appraiser licensing requirements

1991 - licensing started. Lenders and real estate agents were afraid of an appraiser shortage. Verification of experience varied widely among the states. In California you simply "attested" to the experience hours. Many appraisers needed to be licensed at the same time. Many states decided not to require experience reviews. No one knew how many appraisers there were.

1991 - original requirements
Experience: 2,000 hours for certified residential and certified general.
Education: 90 classroom hours, including 7 hour National USPAP,
CE: 10 hours per year.
College class hours: None

1998 - increased requirements
Experience: Res. Cert from 2,000 to 2,500 hours. Gen cert from 2,000 to 3,000 hours
Education: No change except 15 hour National USPAP required
CE: Increased to 14 hours per year
College class hours: None

2008 - increased requirements
Experience: No change.
Education: Cert. Res. 90 to 150 hours. Cert Gen 180 to 300 hours
CE: No change
College class hours: Degree or specified classes

2015 - increased requirements
Experience: No change.
Education: No change
CE: No change
College hours - 4 year college degree require for certified

2017 - possible removal of 4 year degree for certified residential and alternate path for licensed.

Appraisal fees - changes over time

Appraisal fees have not changed much since 1992, except during the recent appraiser shortage, when they increased dramatically for some AMCs and lenders. In response, my non-lender fees increased dramatically as well.

What are customary and reasonable fees when AMC fees can change dramatically based on supply and demand?

With Dodd-Frank and customary and reasonable fees appraisers focused on fees. Some states took fee surveys to set the fees in their states.

But, fees have been going up recently, for the first time that I know of since the early 1990s. When I started my business in 1986, there was a severe appraiser shortage due to significant drop in mortgage loans due to 18%+ interest rates.

However, most appraisers were still charging around $200 to $250 in California. By 1992 (see below) prices had gone up considerably.
When the appraisal market crashed in the early 1990s, there was little or no decline in fees.

In the past, appraisal fees tended to be fairly steady with some increases. Individual appraisal fees varied, depending on their business decisions. Some were lower, some mid-range, and some higher. I was always mid-range. Other appraisers were price leaders, increasing fees whenever they could.

Since AMCs took over about 80% of lender volume, fees varied dramatically among AMCs, even for the same property.

The only stable fees seem to be VA, which increased their fees in the past several years. Whether or not they will lower their fees is not yet known.

URAR fee changes - 1/94 and 7/96 - How do these fees compare with your current fees?

I started my appraisal business in 1986 and charged $195 for a residential form appraisal. Some local appraisers charged more. Fees did not vary much among lenders. They increased during the late 1980s, due to strong demand.

There has always been regional/state differences in fees, which continue today. The northwest (WA and OR), Alaska and Hawaii have always been higher. The rest of the country is lower.

I took the fee surveys below for Appraisal Today. Fees in my area are higher, but were between $300 and $350 for many years until strong recent demand caused some AMC fees to increase and savvy appraisers raised their fees. Also, VA raised their fees to $450.

I am up to about $700 for non-lender fees as I use what borrowers pay for their appraisals as my basis. There are still some local appraisers charging $350.

1/94 Average = $288, range of $200 to $450
7/96 Average = $286 (fees were dropping)

	1/94	7/96
AZ	$275	$245
CA	$306	$288
CT	$256	$296
FL	$246	$275
GA	$288	$250
HI	$436	$425
IL	$242	$253
IN	$237	n/a
MD	$285	n/a
MA	$250	n/a
NC	$254	n/a
NJ	$241	n/a
NV	$312	n/a
NY	$253	$269
OH	$218	n/a
OR	$416	n/a
PN	$225	$250
TX	$312	$300
VA	$295	n/a
VT	$275	n/a
WA	$400	$400
WI	$222	$240

2001 appraisersforum.com survey
URAR fees:

$251-300	46.48%
$301-350	26.95%
$200-250	12.50%
$351-400	8.98%
Over $400	4.30%
Under $200	0.78%

What is your typical appraisal fee? Source: Valuation Review 2016

Fees have increased significantly between 2011 and 2016, and may have started increasing earlier.

2011

Less than $100	0.2%
$100 to $200	3.4%
$200 to $300	27.4%
$300 to $400	45.8%
$400 to $500	17.1%
More than $500	6.1%

2015

Less than $100	0.1%
$100 to $200	0.8%
$200 to $300	8.5%
$300 to $400	45.8%
$400 to $500	29.9%
More than $500	14.9%

2016

Less than $100	0.4%
$100 to $200	1.5%
$200 to $300	5.8%
$300 to $400	39.5%
$400 to $500	32.3%
More than $500	20.5%

Source: Alterra

What is your typical fee today for a 1004 with MC? 2016

2016: Lowest $100, Highest $2,000, Avg. $391.22, Mode $350

Source: Alterra

How has your appraisal fee changed over the past 12 months? 2016

Decreased 12.0%,
Increased 33.7%,
Stayed the same 54.3%

What about commercial and apartment appraisal fees?

In most states, including mine, commercial and apartment fees have gone up some since 2008, but are still low. Demand is lower and, in some areas, larger appraisal firms are bidding low on commercial appraisal bid boards, keeping overall fees low. This has also affected non-lender appraisals.

In 7/96 I took a survey of apartment appraisals, which is a very standard property type without much variations. I do not have any more recent surveys. In my area, fees have gone up some, about $500 or more. What is happening in your area?

My fees (25 units apartments) are about $2,200 for form reports and $3,500 for narratives. Fees for small single tenant warehouses have gone from about $2,000 to $2,500 since 2008.

Apartment fees - 1/94 and 7/96 - How do these fees compare with your current fees?

Apartment form reports - Typical 25 unit property

	1/94	7/96
National avg.	$2,053	$1,907
Midwest	$2,004	$1,798
Northeast	$1,617	$1,550
Southeast	$1,500	$1,600
West (excl CA)	$2,550	$2,375
CA	$2,207	$2,209

Apartment narratives - 25 units, 50-75 page report

	1/94	7/96
National avg.	$2,961	$2,853
Midwest	$2,900	$2,726
Northeast	$2,829	$2,529
Southeast	$2,217	$2,467
West, excl CA	$3,333	$3,406
CA	$3,543	$3,143

Other changes since 1992 - years of experience, appraisal staff

10/92

Years of experience - business owner

Average of "between 5 and 10 years"

This has increased significantly due to few new appraisers since 2008. See below for 2016.

In what year did you begin conducting real estate appraisals? Source: **National Appraiser Survey 2016**, Alterra Group

- Earliest 1951
- Most recent 2014
- Mean 1991
- Mode 1986

Size of company - significant downsizing

Today, the majority of residential appraisal firms have one person. There was significant downsizing due to the appraisal recession at in 1992/93. Appraisal firms became larger during the boom before 2008 due to adding trainees. After 2008, most of the trainees were gone and others quit appraising due to lack of work, takeover of AMCs, etc.

10/92 Number of appraisers in appraisal firm (full and part time)

One	22%
2-3	25%
4-6	25%
7+	27%

Average = 5.4

Support staff (full and part time)
10/92

at least 1	95%
Average number	2.5

What is the future of AMCs?

I don't see lenders taking back appraisal fee panel management. They are not set up for it any more. Lender consolidation has meant that combining fee panels is a big hassle.

There are a few "good" AMCs, such as TSI, which does the appraisals for Quicken loans. Hopefully, they will survive the next appraisal recession. More appraisers will quit working for the "bad" AMCs.

The AMC business model has very high overhead and is too employee-intensive, which is very expensive. Appraising is not a very profitable business because of the high labor costs. For fee appraisal companies, making a 5-10% profit was a good goal.

I am predicting that a lot of AMCs will go out of business during the next downturn.

The excessive scope creep is coming from lenders. This will go away as memory of the Mortgage Meltdown fades, as it always does. AMCs will be less demanding. It really cuts into their profits because of the extra time required.

What about trainees?

Until lenders accept trainees doing appraisals, nothing will change. This never occurred in the past and is completely new. Eventually, the pendulum will swing back to loosened standards.

The AQB can eliminate the 4-year college degree requirement. Specific business and statistics classes are required. This is much more important than having a college degree in something not related to business.

I studied science as an undergrad and never took a business class. I got an MBA after 4 years of appraising as I realized I had an inadequate educational background. (It was easier to get an MBA than an undergrad business degree.)

The future of appraising in 1981 - not much has changed!!

Tom Fryer posted a very interesting article on the NAIFA forum several years ago, written by Lynn Woodward, SRPA, originally published in The Real Estate Appraiser and Analyst, Winter 1981.

Here are a few quotes -

"The appraisal profession may be dying. Although growing, consolidating, and professionalizing, it is not broadening its influence. What is happening to the profession is happening externally without the participants recognizing the potential impact."

"Loss of present appraisal markets to other professions and the demand for non-appraisal analysis which will be provided by firms outside the appraisal industry will limit the appraiser's role in the future. At the Society of Real Estate Appraiser's International Conference in Reno in 1979, Dr. Graaskamp suggested that other professions have real advantages over the appraisal industry in establishing themselves in the analysis report markets and potentially absorbing the appraisal business."

"The secondary market, through the standardized FNMA/FHLMC appraisal form, has defined the appraisal "line by line." The form is not in the control of the appraisal profession, but the form makers - and the appraiser follows."

"The sophisticated investors presently buying real estate equities rely on internal rate of return (IRR), net present value, financial management rate of return (FMRR), modified internal rate of return, risk or probability estimations, and sensitivity analysis models to make investment decisions".

"The appraisal dogma presented by textbooks and other literature stresses traditional techniques of valuation which lack the sophistication of the investors' models."

"The automated statistically based appraisal computer models can estimate the most probable selling price. A reasonable check of the selling price from the database of sold properties stored in the computer, can be accomplished in a few minutes."

What is coming in the future?

We have all known for a long time that the easy tract home appraisals can be done by AVMs. I remember back in the 1980s appraising the same tract home over and over when serial refis were popular. I liked the easy money, but it did not seem fair to make borrowers pay the appraisal fee again and again.

What held back development of AVMs was non-standardized and very limited data. Appraisal reports have always been the "Holy Grail" of data. Now, CU collects a lot of data and many of the fields are standardized by UAD. More fields will be standardized in the future.

MLS data is also readily available, even to the public, online via Trulia, Zillow, etc. Real estate agents have given up their "pocket listing" attitudes and are streaming their listings online.

Fee appraisers are already getting more of the "odd ball" appraisals as AMC staff appraisers take the easy ones. Just like they did when most appraisers were lender staff appraisers.

Non-appraisal information, such as street views are online. "Real time" aerials will be coming soon. Aerial images allow anyone to look for proximity to freeways, lakes, etc. Building permits are increasingly online as are zoning regulations.

When will full appraisals still be needed? Fannie needs to do more risk analysis first to determine which properties don't need full appraisals. Their investors must be willing to purchase the mortgages. They will lead and others follow. CU will help. Conforming tract homes with high LTVs will be gone first.

How long before most full appraisals will go away? No one knows, but it will be slow as Fannie is very conservative. It depends on how many years you plan on doing full appraisals, which is mostly a function of age. If you are approaching retirement, you won't have to worry. I am 74 and have been cutting back on appraisals for the past 4 years, so it will not affect me.

When will appraisers be needed for desktop appraisals, and other valuation products? This is the future. Many lenders have wanted appraisers to do them over the years, but most refused. This is your best alternative if you don't want to do difficult appraisals and/or non-lender work.

Survival for the residential appraiser: how I learned to stop worrying and love the AVM that put me out of business!

by Barry Bates

Background to the Déja Vu: How could appraisers become extinct just a few years after a monumental housing crash?

My last article in Appraisal Today identified the probable rollout of steroid AVM technology and maneuverings of the government sponsored enterprises (GSEs; Fannie, Freddie, Ginnie, etc.) that will likely cut full appraisal assignments across the mortgage process by 70%-90% within 10 years.

It sounded a little like the little boy who cried "wolf"(or that I missed my morning Cymbalta) because the first advent of AVMs in the 90s met with a cool reception on the part of lenders.

So I also explained why enthusiasm was lacking, and presented some evidence to show that a second AVM wave-to be accompanied by artificial intelligence that will read the age of the roof from a 3-day-old satellite photo-is already being facilitated by a proliferation of new agency loan programs that require no appraisal.

This article deals with "resi" appraisers and their future options, howbeit limited, in the mortgage market.

Future articles in the same series will address appraisal services to professionals (doctors, lawyers, engineers, etc.), the shrinking regulatory structure (including a critique of the structure itself based on personal experience and research). Also, services that appraisers can train themselves to perform, involving residential real estate, but not necessarily valuation.

Interleaved throughout (including this article) are ideas for entirely new business ventures that former appraisers might pursue in order to serve markets presently in formation. Much of my research has consisted simply of interviews with mortgage industry participants from my past who are not yet wearing diapers; some them have risen t•o lofty positions having a unique view of the mortgage landscape.

Now is the time to assess your business strategy

My paranoia with respect to the future of our profession stems from 45 years in and out of the mortgage business, mostly as a chief appraiser, but later as a valuation manager in mortgage-backed securitization.

But, my experience taping houses is close to my heart and leads me to believe that, if you are a residential appraiser, NOW is a good time to reassess your business strategy if you want to continue to enjoy residential real estate analysis, a decent annual income, and some fresh air every once in a while (tire-kicking in the field).

Given current talk about another property bubble (to be perhaps heaviest in commercial), and with a decidedly business-friendly crew (of pirates?) in the White House, it's a good time, too, to restock your bomb shelter (conforming subterranean subdivisions are all the rage; *Google Texas company* that builds bomb shelters or *Trident Lakes doomsday prep, or terravivos.com*).

A look back at the recent housing crisis

To winnow out indications of where and how an appraiser will survive, a refresher in the housing crash is in order. Lender attitudes toward collateral risk were negatively influenced by the role of appraisers in the collapse, despite the fact that street-level valuers were only a tiny link in a chain connecting loan originators to securitizers, who were sometimes the same person.

To pick up everything you need to know about the 2007-2009 confidence crash of the housing market, all you need to do is rent the movie or read the book. Yep, that would be *The Big Short*, a paperback by Michael Lewis, possibly the greatest financial journalist of the new millennium; and a movie with a huge cast of millennials pivoting around Christian Bale as Michael Burry, MD.

If there was one historical development in the mortgage world that outstripped the separation of origination from warehousing, it was the newest available derivative available on Wall Street in 2007. That was the *credit default swap*, which made it possible to pour your money into a risky investment, but buy insurance to cover it if it failed to work out.

In other words, you could bet on yourself and against yourself at the same time. While most small investors holding CDOs (monster coagulations of securitized loans known as Collateralized Debt Obligations) went down the drain, the big smart money made bigger smarter money by betting against them. There oughta be a law.

Among the colorful characters in The Big Short are, of course, a lot of financial lawyers, one of whom is heard to say, *"Truth is like sh*t; it stinks badly, and we have to get rid of it fast."* This is the amoral principle which has risen to the top of the global financial system along with a legal, sales-focused management mentality permitting, nay, encouraging, by law, business and government, to place company shareholder ROI above customer investment security.

Appraisers played their part by drinking the offered Kool-Aid that convinced them to cosign the age-old proposition that home price appreciation would cover any current overvaluation. A concomitant old saw, so negative that even I could never stand using it, has taken on a decidedly creepy ring of truth: "America is still a "melting pot"; the scum floats to the top and everybody on the bottom gets burnt."

How the crisis affected residential appraisers

Residential appraisers in the trenches of the crisis weren't certain of the causes of the meltdown, but they had a sense of impending doom. They knew one thing: they'd get blamed for it. And they were, despite the enabling collusion of borrowers, mortgage originators, investment bankers, insurers and guarantors.

At the top of the pyramid, in a regulatory sense, were the stock/bond rating agencies (Fitch, S&P, Moodys, AMBAC, etc.). They maintained and certified the conveyor belt that converted thousands of bad loans into securities that shortly impoverished thousands small investors, caused a 30% drop in home values, resulted in the loss of 8-9 million jobs and left 12 million homeowners in houses worth less than the mortgage balances.

Certainly one theoretical problem puzzled appraisers, namely, what happened to the relationship between cost and price? After subtracting construction costs and land value, there was a huge pile of cash left over in these home sale transactions that couldn't be sourced.

Theory said it should be reflected in land value, but recent land sales didn't come close to supporting final prices. Unfortunately, we shrugged and assumed it was just the appreciation that accrued during the lag between comparable sale closing dates and our valuation date.

What if this happens again?

More recently, appraisers have started asking themselves, what if this happens again? How can I avoid getting caught up? Then they went back to work and forgot their own foreclosure.

Their tattered reputation in the mortgage industry encouraged regulators and originators to throw more underwriting responsibility onto appraisers by adding economic form fields.

This further reduced originator liability by creating the new appraisal management company intermediary model. Supposedly this was to prevent appraiser abuse, but, in practice to ply appraisers on specious grounds for higher numbers by threats.

It became possible for one "low appraisal" to put an appraiser out of business.

The White House and GSE's risk sensitivity

A new business-friendly White House could be counted on to dismantle a portion of the post-crash preventive regulations and statutes, clearing the way for another period of unbridled lending to borrowers with little capacity to repay.

Of course, this decline in risk sensitivity was made possible in the creation of the GSEs in the 30s-40s to securitize mortgages. For the first time, mortgage originators were no longer required to hold mortgages for their full terms, but, could sell them (and their risk) to third parties before the ink was dry.

There was an *implicit GSE guarantee* that the government would bail out buyers in the event that a well-known noxious organic substance impacted the air-movement device.

"Incidentally", the move allowed the loans to be moved off the government balance sheet, making the national debt look lower than it really was.

Countrywide Financial jumped into securitization in the 60s, and the rush to glory began, in 1970, the investment banks smelled cash. In 1970, Salomon Brothers issued the first "private labeled" MBS (mortgage backed security) containing no GSE mortgages. It fell flat on its face.

HVCC and Dodd-Frank Provided NO Appraisal Independence

By the late 80s, mortgage lenders, whose memories are no longer than those of the general public, were again thinking that if the residential appraiser could be removed from the process, the origination process could be radically accelerated and disruption costs significantly reduced.

(Until recently, science had posited the conclusion that the creature with the shortest attention span is the goldfish, at 9 seconds. A 2015 study has now placed humans at 8.)

This thinking was evident in the late 80s and 90s when AVMs appeared on the scene. But, regulators were leery of the technology, geographic coverage was spotty and a lot of the megadata unreliable or just plain missing. When originators discovered that using an AVM made it impossible to change the value after it was estimated, the plan was aborted.

AMCs did not reduce risk

Today, regulators think they may have strengthened existing prohibitions against pressuring appraisers through the *TILA-RESPA* Integrated Disclosures (TRID) by preventing any change to appraisal fee (or, by extension, the property value estimate (with some loopholes-er, exceptions) once the disclosure has been made to the borrower.

But, the tightening of loan disclosure delivery timeframes would not have been necessary to lower pressure if replacement of mortgage brokers with appraisal management companies (AMCs) had been a success.

Intermediary between appraiser and lender client - problems

Mandated through the promulgation of the Home Valuation Code of Conduct of 2008 via the Freddie Mac GSE and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the placement of an intermediary between the appraiser and lender-client had problems.

It simply made it possible via the internet to blacklist an appraiser with a number of major lenders/originators rather than with a single mortgage broker or originator.

The assumption that, unlike a mortgage broker, an appraisal management company would not have "skin in the game" was false. For financial success, the AMC was beholden to the lender-client from which it collected not only appraisal orders, but marching orders. A shockingly obvious conflict of interest was simply overlooked.

It wasn't long before some AMCs had tacit agreements with lender-clients that if the appraisal did not support the loan request (amount), the fee would be refunded and, in some cases, retribution against the appraiser would follow. VERY HARD TO DOCUMENT.

So the inevitable continuing profit pressure to develop a non-controversial value estimate has resurfaced. The GSEs are positioned to develop an extremely robust AVM bolstered by artificial intelligence, and satellite mapping data with new ways to evaluate property views and potential negative externalities. To smooth the path of implementation, **only a low profile needs to be maintained with respect to the AVM. No big announcement or rollout process, just the quiet continuation of new loan programs with appraisal waivers (avoiding the word "appraisal"). Eventually there was a GSE rule change that broadens the use of the AVM to wider categories of loans. (Last month's article details some of the loan programs already implemented or changed to increase use of valuation products other than appraisals.)**

Yet the powers behind this probable development (see prior article) fails to remember the deal-killer that turned up last time. What if the AVM runs low?

Low AVMs

Well, since AVM algorithms are proprietary and protected by copyright, the only way to know if it has been tampered with is to reverse-engineer the model and test it. Only a few AVM testing labs currently exist (or maybe only one: Lee Kennedy's AVMetrics).

What would be the motivation, other than a court order, to look under the hood? Perhaps more urgently, from the perspective of a mortgage originator or regulator, which fox could be trusted to guard the henhouse?

Right: a quasi-governmental agency, like a government sponsored entity (GSE); it already has the credibility to ward off inquiries.

What value do mortgage lenders see in appraisers today?

The implication in all of this is that the value mortgage lenders see in appraisers today (given the changed mentality in the c-suite) an opportunity to "renegotiate" the value conclusion.

Appraisers have never been willing to modify a value conclusion without one hell of a good reason. After all, their professional mandate is impartiality.

There are still a few (some say an increased number of) appraisers who will do what the lenders want. But, convincing an appraiser that s/he's wrong in the conclusion s/he has already reached through diligent effort has always been, and should always remain, a difficult process in the absence of hard data support.

Assuming it does continue in a traditional way, most lenders would rather keep the pushback option open than be bound to an automated final number, unless "the fix is in" with the AVM: a tough technical problem, but, not an insoluble one.

All this is written in the hope that the public realizes that most appraisers are honest. In those rare cases where they "roll over" without sufficient reason, it's fear and intimidation, not a bribe, that causes failure of integrity.

Blacklists and other threats to livelihood are the weapons still at the disposal of single-minded, sales-driven mortgage policymakers.

What does this speculation mean for appraisers?

Whether or not any of this speculation about a Killer AVM or the fact of weakening regulation is truly warranted, it behooves the residential appraiser to be ready to find another job or retool the existing one to match a future dystopia in which "truth has indeed become sh*t for immediate disposal".

As always, the appraiser has one, and only one, powerful weapon against intimidation: the withholding of services. There is no defense at all in a lending environment where 90% of all mortgage appraisal work is purely optional as a matter of GSE and regulatory policy.

How much lending work would be left for the current 49,218 certified residential appraisers?

According to HMDA data (at consumerfinance.gov), there were 6,223,787 first-lien mortgages (purchase and refi) on owner-occupied, 1-4 unit properties originated in the US in 2015.

Assuming that new GSE programs have already created waivers (see prior article) for 10% of those mortgages, and certified general appraisers were prohibited from accepting residential assignments (what a great idea!), each appraiser would enjoy 114 assignments per year and an annual income of 114 x $450 (the dream average fee), or $51,300.

I ballparked this number, believe it or not, before I went to salary.com to find that the real median annual salary as of April 27, 2017, was $50,700. Sorry for the margin of error.

Sounds low, doesn't it? That's because 114 appraisals per year equates to only 9 full appraisals per month.

Author’s Side Note: If you live in Daly City, California (next to San Francisco), across from the Arby's, you might need to write 22 reports in order to pay the $3,291 monthly rent on your 1,180SF, 3BR apartment at the stylin' new La Terrazza. The ad repeatedly refers to the location as San Francisco. It's actually in Colma, California, a small San Francisco satellite town with six large cemeteries and a golf course. Note to golf course developer: the dead do not play golf.

A new 1,217SF, 2BR apartment at the Alchemy by Alta in the 200 block of Buchanan in San Francisco [Hayes Valley, a C+ location] will run you $5,875 per month; you might have to hire a trainee!)

Obviously, the loss of even 70% of mortgage appraisal volume, let alone 90%, will devastate the ranks of appraisers, especially those who were planning on a few more years of work before retirement, or those newly entered (or planning to enter) into appraisal work.

The remaining cadre, except those who, like the publisher of this newsletter, have earlier managed to exclude "lender work" from the list of assignments they accept, will be scrambling to redefine themselves.

Moreover, trainees who have already been unable to find the required supervisory appraiser might suddenly find it impossible.

End of Author’s Side Note.

But, all is not lost!!

Areas Where Mortgage Entities Will Still Need Appraisal Expertise

There are those who say that an appraiser's "geographic competence" is a phantom of the past. That anything you know about your market or your property can be found out on the internet in 60 seconds.

Not true, at least not yet: Reports quantifying the effect on value of detrimental adjoining uses not discoverable without local or immediate knowledge.

The high-rez or infra-red satellite may be able to see that an adjoining property is in poor condition, but it can't see the flourishing meth lab in the basement.

An appraiser who can drive by or who has inspected nearby properties in the past will know or can discover such factors. This is where appraisal blends into detective work.

Is the lender/client looking for a way NOT to make a loan? Check out the High Technology Crime Investigation Association. A few courses may add an investigator cert to your achievements and broaden your scope of practice. Maybe even look at the American Board of Medicolegal Death Investigators (ABMDI).

(Rhetorical question, I hope: Has everybody already discovered diedinhouse.com? As an investigator for the State, I never researched a house without checking this site.

Just this minute, I looked up the retirement house my wife and I bought here in Pittsburgh last November, and where we are currently residents. At least one death noted, possibly more, but then you pay for the info.

I learned that in PA, death in a home is not legally considered a "material fact"; all the more important to show that you know and have investigated! (Our house was built in 1930. I'd be creeped out if somebody DIDN'T die in the house!)

How many other little property details might have a temporary or permanent effect on market value? Last weekend I found that a chainlink fence behind my property line is pushing over a very heavy tree into the highway right-of-way 60' below.

Are the fence and the tree located out of my area of liability? Why did the old chainlink collapse in the first place, and why is it 20' out of its original position?

(Appraisers always buy crappy houses for themselves. It gives them a lifelong analysis project and a way to collect damages from the seller.)

Hybrid valuation reports.

We all know that combo inspection / AVM and inspection / valuation reports are already in the market that qualify as "evaluations" under the Interagency Appraisal Guidelines. This is the reason for the new push for an increase in the de minimis thresholds.

Some use an appraiser for the inspection and another appraiser for the valuation portion. Some are actual appraisals with the inspection done by an appraiser or trainee acknowledged for significant assistance.

When I started my own valuation business (InsideValuation, now a part of LRES), I learned how to program PDFs and created a commercial BPO that could be signed by an appraiser, a commercial broker or a CCIM. I just reworded the certification to fit all three.

We started to market the whizbang form (**you can have it or use it; it is posted on the paid subscriber page, underneath the newsletter links**), but ran up against a problem that will be faced by appraisers "repurposing" their businesses.

Some potential clients don't know what they need. Some lions have thorns in their paws and are completely unaware. In my case, my capital partners just wanted to put more marketing effort into boring commercial BPO. Indeed, the company ended up at about $8M in annual sales.

Collateral Risk Reports

In the Dismal Science (economics), believe it or don't, the jury is still out with regard to whether the house being sold, i.e., the security for the loan, has ANY effect on its market value. While the jury deliberates, the markets have decided that it must, and "collateral risk" has become a stand-alone industry.

The general idea is that poor maintenance on a refi or a family room added without permits affects the prospect of loan default because people who are careless about stuff like that are often careless about their finances and are more likely to miss mortgage payments or quit making them entirely.

You can even manufacture a correlation by finding a loan sample where a comparison of houses with and without the factors confirms a relationship. Yet it's also possible that the factors are unrelated and some other undiscovered feature is responsible.

Since securitizers and originators will likely claim that the new AVM-on-steroids will push collateral risk into acceptable limits (say, under 5% of loan amount), nervous back-market entities will want to make sure that the factors exist and will want to see other variables that they believe are also related to loss given default.

Like the shiny brass pole in the middle of the family room or why the loan-to-value ratio is 90% when the borrowers had income to support a 70% loan.

The vendor that can make a plausible argument that its selected variables are the best indicators, and that they have a white paper proving the correlatios.

Such report could become a staple requirement of every AVM conclusion, i.e., a collateral risk score over 610 (might as well structure it to look like a FICO score, right?).

There are a couple of appraisers/entrepreneurs noodling over this product at the moment, but there is probably room in the market for several competing models.

Environmental Reports

Our new place (circa 1930) in Pittsburgh has a water supply line connecting the house to the main line in the street with a pipe made out of-guess what-lead, of course.

Effect on value? Who knows, but there's going to be bond money available to homeowners to replace the line at very low hard-dollar outlay with a loan that could run with the land for 25 years.

The borrowers and municipal loan guarantors will need appraisals, or, preferably, a report that can guarantee or bond a value that will support an addition lien of $7,500 on title. Why pay $450? USPAP compliance optional. Maybe.
Rebuttal Reports / Advocacy Reports.

Nothing drives Realtors®, who are crazy already, crazier than having an appraisal come in $10,000 short of the contract price, especially when the buyer doesn't have enough cash to negotiate. Lenders often advise sellers and buyers to submit a rebuttal if they think the value conclusion is low, which, of course, it always is.

Agents and buyers don't have the necessary skills-or the time-to write a coherent valuation rebuttal. Sometimes, these rebuttals actually work; in some cases, it's just because the buyer made the effort.

Some appraisers are considering an abbreviated rebuttal report when the other appraisal really IS low, or an "advocacy report" when the other appraisal is reasonable, but there are comps in the market that cast doubt on the conclusion. The latter report type does not estimate value.

Estimate of Reasonable Maximum Loan Amount

Need I say more? Why estimate market value for a lender, which creates an appraisal by legal definition and invokes USPAP (as well as and a panoply of state laws and regulations), when you can just estimate maximum loan amount? If you're criticized for just playing with percentages, don't show the percentages. Let them eat cake!

All of the potential products above are either in development, being proposed to or by one or more loan originators, or are the new twinkle in the eyes of an appraisal partnership that is considering a major overhaul in its business model. Remember that you don't have to be a genius, a salesperson or an entrepreneur to capitalize on the ventures and ideas described above. All you need to do is produce the products themselves to make that decent living into perpetuity.

Whiskey and fresh horses for our men and women!

About the author

Barry Bates was born near Portland, Oregon, but grew up in San Francisco. He entered the appraisal profession in 1972, after four years in the US Army, and another four at the University of California, Berkeley, where he majored in English Literature and minored in Slavic Languages and Criminology.

Between 1972 and 1986, he served as a staff residential appraiser. Over the years he had various appraisal management positions with banks. Bates also worked for Countrywide Securities and Hansen Quality Loan Services, analyzing portfolios for mortgage-backed securitization.

By 2004, he was Property Valuation Manager for Morgan Stanley Mortgage Capital in Boca Raton, Florida. In 2006, Bates founded InsideValuation, a provider of commercial broker price opinions and IAG evaluations, which was sold to Lighthouse Real Estate Solutions.

At 71, Barry has had wide-ranging experience and a technological perspective in a fast-paced career that serves as a testament to the fact that he has never been able to hold down a steady job.

He now lives in Pittsburgh, Pennsylvania with his wife, Kathleen and their two dogs, where he writes for real estate publications and, in his own words, tries to get into more trouble (in 2008, he filed whistleblower suits against MERS (on behalf of county recorders) in 12 states, all of which failed miserably.

Contact Barry at barrettbates@gmail.com. Note: it may take a while for him to respond as he does not check his email obsessively any more as he is sorta retired…

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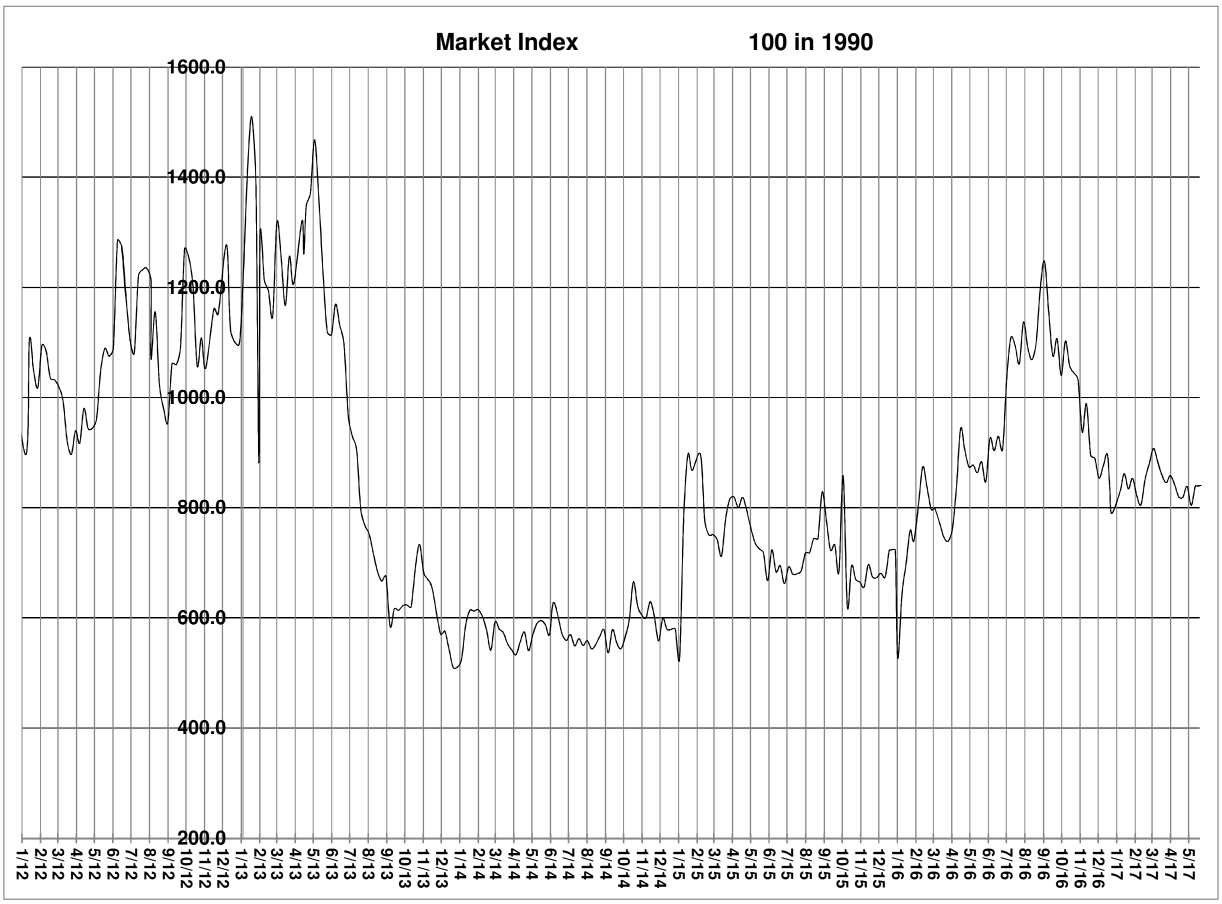
MBA Loan Volume Application Index 1/12 to 5/17

As you can see below, between 2012 and today, volume peaked in early 2013, declined, then peaked again in 8/16. A good demonstration of the ups and downs of mortgage lending.



The survey covers approximately 75 percent of all U.S. retail residential mortgage applications, and has been conducted weekly since 1990. Respondents include mortgage bankers, commercial banks and thrifts. Base period and value for all indexes is March 16, 1990=100.

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