



Policy Position: The Importance of Accurate Appraisals Performed by Independent Appraisers

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Issue: Accurate appraisals are one of the fundamental components of the loan decision because a borrower's credit and willingness and ability to repay are only two of the three 'Cs' (credit, capacity and collateral) used by lenders to make lending decisions. In the event a borrower is unable to meet the payment obligations of a loan, the underlying property serves as the collateral for the obligation. Appraisal estimates are expected to be unbiased reports. With increased concerns about lending practices brought about by current market conditions and the rise in delinquencies, anti-predatory lending proposals with a focus on altering existing appraiser and appraisal standards are keen on legislators' minds. MBA is especially concerned that policy-makers will increase industry regulation where it already exists to ban coercion on appraisers to artificially inflate values and expose lenders to additional liability and expense.

Position: In order to ensure appraisals are accurate and performed by independent appraisers, MBA believes:

- ***Lenders, real estate brokers, borrowers and appraisers are best served by ensuring that the existing principles of USPAP are obeyed.***

Several parties to the transaction, including but not limited to the real estate broker and mortgage broker can benefit from artificially inflated appraisals, because they receive commissions from the value of the sale or the loan. It is crucial for the residential real estate market as a whole, that appraisers remain independent and objective in their analysis. That independence must be enforced by the ethical behavior of appraisers and a staunch unwillingness to bow to pressure, blatant or otherwise, from those parties with which they do business. Regardless of competitive pressures in the marketplace, appraisers are required to comply with the Uniform Standards of Professional Appraisal Practice (USPAP) and are responsible for their work product.

- ***Any new federal appraiser coercion law must accomplish two things.***

Any new federal law addressing appraisers should: 1) include all of the principal parties to the real estate transaction (including real estate brokers, mortgage brokers, lenders and borrowers), and 2) use objective, legally defined terms to describe pressure ("extort, bribe or coerce"), rather than unclear, subjective terms like "instruct," "influence" or "intimidate."

- ***More adequate funding of state appraisal boards is needed.***

MBA supports the adequate funding of state appraisal boards to allow for sufficient oversight and enforcement of the appraisal process. Ultimately, the regulation and oversight of the appraisal industry rests with the appraisal boards in the states – often overlooked regulatory bodies – that, without adequate funding, cannot perform their regulatory function. In a 2003 report, the Government Accountability Office (GAO) surveyed the appraisal agencies in all 50 states, the District of Columbia and the U.S. territories, and the agencies reported “funding shortfalls hindered their ability to enforce compliance.”¹ Industry experts say nothing has changed since then. MBA is concerned most agencies lack necessary human capital to investigate appraisal fraud, and many have expressed a need for more resources to address litigation.

- ***Increased efforts to detect and deter fraudulent schemes are needed, including a national mortgage fraud database and the creation of a national valuation registry.***

MBA recognizes that mortgage fraud is a burgeoning crime that is impacting more and more companies and communities. Recent statistics from the Federal Bureau of Investigation (FBI) illustrate just how quickly the problem is growing: the FBI had 436 mortgage fraud investigations in September of 2002. Currently, it is handling well over a thousand cases, an increase of over 237 percent in less than five years. In response, MBA supports increased efforts to detect and deter fraudulent schemes, and believes this is best accomplished by increasing lenders’ ability to quickly and efficiently share information through a national mortgage fraud database and the creation of a national valuation registry.

Rationale: With increased scrutiny of lending practices brought about by current market conditions and the rise in delinquencies, some anti-predatory lending policy proposals also alter existing appraiser and appraisal standards. MBA is especially concerned that policy-makers will react to reports of appraiser coercion by increasing industry regulation (where it already exists to ban the practice) and expose lenders to additional liability and expense. MBA opposes all fraud that affects the mortgage industry, and it is important to understand that mortgage lending institutions do not benefit from inflated appraisals.

¹ U.S. Government Accountability Office, GAO Report to Congress, *Regulatory Programs: Opportunities to Enhance Oversight of the Real Estate Appraisal Industry*, GAO-03-404, May 2003.

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Additional Background:

When a consumer applies for a home loan, the lender evaluates, among other things, the borrower's creditworthiness, income and debt, and the appraised value of the property. A lender relies on an appraiser's assessment of the value, condition and marketability of a property in determining whether the property provides adequate security for a loan. If an accurate value of the property is obtained and the loan goes into default, lenders should be able to recoup most of their loan principal, interest and advances through the foreclosure of the collateral, or home. If the appraisal contains inflated, inaccurate or material omissions related to the value of the property, the lender will likely suffer a greater loss if the loan goes into foreclosure. Furthermore, a borrower who obtains financing based on an inflated value may be less likely to continue making payments when he or she discovers the value of their home is lower than the outstanding loan balance.

Title XI of FIRREA Covers Appraisal Quality, Qualification and Oversight

As early as 1986, Congress issued a report² concluding that faulty and fraudulent appraisals were an important contributor to the losses that the federal government suffered during the savings and loan crisis. In response, legislators passed Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) to address both the quality of appraisals and the qualifications of appraisers. Title XI requires that real estate appraisals used in connection with federally related transactions be performed (1) in writing, in accordance with uniform professional standards, and (2) by individuals whose competency has been demonstrated and whose professional conduct is subject to effective supervision. Title XI also created a 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.

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 conduct the certification and licensing of appraisers, including setting education and experience requirements that, at minimum, must meet AQB criteria for certified appraisers and enforcing compliance with appraisal standards. Federal financial regulators (the Federal Reserve Board, FDIC, OCC, OTS and NCUA) also issue appraisal management requirements for the financial institutions under their jurisdiction and monitor compliance with management plans established to satisfy their regulations.

² Impact of Appraisal Problems on Real Estate Lending, Mortgage Insurance, and Investment in the Secondary Market, H.Rep. 99-891 at 4-6 (Sept. 25, 1986), House Committee on Government Operations, 99th Congress, 2nd session.

USPAP Establish Requirements for Appraisers and Users of Appraisal Services

The ASB's minimum standards for appraisals are contained in the Uniform Standards of Professional Appraisal Practice (USPAP) which, under Title XI, apply to all federally related transactions with loan amounts over \$250,000. USPAP directs appraisers to conduct their inspection and their relationship with the party that requested the appraisal under ethical guidelines. Appraisers are expected to be knowledgeable about the neighborhood where they operate, impartial in their judgment and ethical in their conduct. The federal regulators require that all appraisals prepared by appraisers for eligible federally related transactions conform, at a minimum, to USPAP, that they be written, and that they contain sufficient information and analysis to support the institution's decision to engage in the transaction. In addition, regulators may take informal and formal enforcement actions, including prohibition, removal, and cease and desist orders, and imposing civil money penalties against lending institutions that violate their appraisal regulations.

Appraiser Complicity to Inflate Values Is Fraud

A recent survey of appraisers³ found that 90 percent of appraisers reported pressure from mortgage brokers, realty agents, the consumer and others to raise property valuations to enable mortgage transactions to be closed at a false loan-to-value (LTV) ratio. That was up from a similar survey conducted in 2003, in which 55 percent of appraisers reported attempts to influence their findings. While appraisers are compensated by flat fees that vary based on the type of appraisal (such as a "full" Uniform Residential Appraisal Report) that the lender orders for a given loan, other parties to the transaction are compensated by commission, such as the real estate broker and the mortgage broker. Unscrupulous parties to the transaction may attempt to artificially increase the appraised value of a property to increase the sale or loan amount, thereby increasing their profit. While it is sometimes very difficult to distinguish a faulty or inaccurate appraisal from a fraudulent one, fraud in the appraisal process can be perpetrated when an appraiser succumbs to pressure to establish an inflated property value. A fraudulent or a bad appraisal will often apply inappropriate comparisons of properties, might overlook more relevant comparable properties or fail to identify poor conditions or repairs that are needed at the subject property. When an appraiser does intentionally establish an inflated property value, the appraiser is complicit to fraud and is in violation of USPAP.

**MBA Staff Contacts: Corey Carlisle
 (202) 557-2860**

**Andrew Szalay
(202) 557-2941**

³ October Research Corporation, National Appraisal Survey 2006.