NATIONAL ASSOCIATION OF REALTORS®

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REALTOR®

430 North Michigan Avenue
Chicago, Illinois 60611-4087
312.329.8540 Fax 312.329.5962
Visit us at *www.REALTOR.org.*

Coldwell Banker Residential Brokerage
2801 Gateway Drive, Suite 180
Irving, TX 75063
972.582.9100 Fax 972.582.9157
Email: charlesmcmillan@prodigy.net

Charles McMillan, CIPS, GRI
President

August 04, 2009

The Honorable James B. Lockhart III
Director
Federal Housing Finance Agency
1700 G Street, NW
Washington, DC 20552

Dear Director Lockhart:

I am writing on behalf of the 1.2 million members of the National Association of REALTORS® (NAR) regarding your agency's July 22, 2009, Update on Enterprise Implementation of the Home Valuation Code of Conduct (HVCC). NAR supports the independence of appraisers and the integrity of the appraisal process. We applaud your efforts to clarify misinformation surrounding the HVCC but we disagree that the Code is appropriately dealing with the controversy that has surrounded appraisers and their property valuations.

The National Association of REALTORS® is America's largest trade association, including NAR's five commercial real estate institutes and its societies and councils. REALTORS® are involved in all aspects of the residential and commercial real estate industries and belong to one or more of some 1,400 local associations or boards, and 54 state and territory associations of REALTORS®. NAR has approximately 30,000 appraiser members from across the country and approximately 750 have earned our Residential Accredited Appraiser (RAA) and General Accredited Appraiser (GAA) designations.

The Code has been in effect for several months and our members report that it is causing delays in closings and canceled sales. According to a survey of our members, 76 percent of respondents said the length of time to obtain a completed appraisal report increased after May 1, 2009. More than one third of REALTORS® have lost at least one sale because of a delay in the appraisal process. At the same time, respondents who identified themselves as appraisers said their time frame to submit an appraisal report has decreased and half of these respondents say this impacts the quality of the appraisal report. Finally, consumers are paying more for delayed appraisal reports that may have quality issues. More than two thirds of those surveyed indicated that the cost to the consumer has increased sometimes by more than $100 for an appraisal.

Anecdotally, NAR has received complaints from brokers, appraisers, and even lenders supporting the results of our survey. One appraiser recently contacted NAR about receiving a request from an appraisal management company. The same day the request was received the REALTOR® called looking for the full appraisal report because closing was in 24 hours. The appraiser worked hard to get the report completed and returned it to the AMC in time for closing. Unfortunately, the AMC did not deliver the report to the lender in a timely fashion, which delayed the closing for 2 weeks. A REALTOR® member recently stressed to NAR that AMCs would not be using appraisers who lack geographic competency if HVCC were not in place. Finally, one lender shared a story with NAR staff about a refinance that included one foreclosure as a comparable and another comparable that was several miles away. As a result, the appraised value of the home was too low for the homeowner take advantage of the low interest rates to refinance their home.

Jack Guttentag, Professor of Finance Emeritus at the Wharton School of the University of Pennsylvania, recently said "the HVCC 'cure' for the appraisal problem of overvaluation has been implemented in a market in which the problem has become undervaluation, and the code is making that problem much worse. When markets return to normal, there will be time to reconsider how appraisals can be made independent without disrupting business relationships that have served borrowers well."[1] NAR continues to call for an 18-month moratorium on HVCC to address unintended consequences while the real estate markets stabilize.

Thank you for your time and consideration of this matter. Correcting the unintended consequences of the HVCC will ensure a stable real estate market. If you have any questions or concerns, or if I may be of service to you, please do not hesitate to contact me or our Senior Regulatory Policy Representative, Jerry Nagy, at 202.383.1233 or jnagy@realtors.org.

Sincerely,

Charles McMillan, CIPS, GRI
2009 President, National Association of REALTORS®

cc: The Honorable Andrew Cuomo
Attorney General
The Capitol
Albany, NY 12224

[1] Washington Post, August 1, 2009.

New Appraisal Rules Backfire in Down Market

By Jack Guttentag
Saturday, August 1, 2009

Enacting rules to curb abuses that arose during a housing bubble, but which don't take effect until the succeeding financial crisis, can easily do more harm than good. This is the case with new rules requiring that property appraisals be insulated from pressures exerted by any of the parties with a financial interest in an appraised value. Those parties are primarily lenders, mortgage brokers and real estate agents.

Appraisals are informed judgments regarding the value of specific properties. They are not perfect because appraisers must work with incomplete information. Further, appraisers are subject to bias, especially when less-than-complete information is available to them.

During periods of rising house prices, such as 2000 to 2006, many appraisers erred on the upside because they were part of a community that expected further price increases. This tendency was sometimes reinforced by pressures exerted by lenders, real estate agents and mortgage brokers. None of them wanted to see deals torpedoed by appraisals below the prices buyers had agreed to pay.

In late 2007, New York Attorney General Andrew M. Cuomo sued the appraisal subsidiary of title insurer First American for allegedly conspiring with Washington Mutual, a major mortgage lender at the time, to inflate appraisals. Because WaMu sold a large portion of its mortgages to Fannie Mae and Freddie Mac, Cuomo embarrassed the agencies into issuing a Home Valuation Code of Conduct, or HVCC. The code declared that the agencies would purchase only mortgages supported by an "independent" appraisal.

The objective of HVCC was to insulate the appraisal process from influence by any of the parties with an interest in the outcome. Mortgage brokers and real estate agents could no longer order appraisals, and lenders had to obtain appraisals in some manner that prevented them from exercising any control.

The problem with this well-intentioned rule is that it was issued in December 2008, to become effective May 1 of this year, squarely in the middle of the worst housing market since the 1930s. With house prices declining, the upward bias in appraisals that had prevailed during the bubble morphed into a downward bias. Many deals are not getting done because appraisals are coming in too low, and the HVCC is seriously aggravating the problem.

To protect themselves from liability, most lenders are ordering appraisals from appraisal management companies, which act as intermediaries between lender and appraiser. The appraisal management company selects and pays the appraiser, receives and evaluates the appraisal, and passes it to the lender, which has no direct contact with the appraiser.

Because the management companies operate nationally but do not have appraisers everywhere, more appraisals are being done by people who are not familiar with the local market. Appraisers working for management companies are also paid less per appraisal than independents, which may induce them to invest less time. Less knowledge by appraisers means more scope for bias, and in a declining-price market, the prevailing bias is toward lower values.

Intermediation by appraisal management companies also lengthens the period required to complete purchase transactions. People involved in the process tell me that it can add an extra week. In an increasing number of cases, the paperwork doesn't get done by the due date specified in the contract or before the buyer's mortgage lock expires, potentially derailing the transaction.

The objective of the HVCC was to prevent pressure being imposed on appraisers to raise values. But the code also prevents the loan officers, mortgage brokers and real estate agents who work with borrowers from pressuring appraisers to get work finished in time to meet a deadline. Further, they can no longer keep their clients informed about the status of an appraisal because they are no longer in the loop.

Loan officers, brokers and real estate agents used to have access to informal value opinions from the appraisers with whom they worked. Such opinions allowed them to abort house purchases and refinances that clearly would not fly because of inadequate property value. With this source of information now unavailable, deals that previously would have been screened out early are now going through the system, only to be rejected later, imposing needless costs on everyone involved.

The HVCC has also pretty much eliminated the ability of a borrower to use the same appraisal with multiple lenders. Before the code, mortgage brokers could use one appraisal with any of the wholesale lenders with which they dealt, and lenders sometimes accepted appraisals ordered by others. Today, brokers are out of it and lenders using appraisal management companies will not accept appraisals ordered by other lenders because they cannot be sure that the other lenders are following the HVCC rules. The upshot is that borrowers often have to pay for more than one appraisal.

In sum, the HVCC "cure" for the appraisal problem of overvaluation has been implemented in a market in which the problem has become undervaluation, and the code is making that problem much worse. It should be scrapped. When markets return to normal, there will be time to reconsider how appraisals can be made independent without disrupting business relationships that have served borrowers well.

Note: I am grateful to Kevin Iverson for his insights.

Jack Guttentag is professor of finance emeritus at the Wharton School of the University of Pennsylvania. He can be contacted through his Web site, at http://www.mtgprofessor.com.

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