

“Federal Affairs Update”

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Recent Successes or Acknowledgements

- Federal

- Dodd-Frank includes most significant appraisal reform in two decades
 - Customary and Reasonable fees
 - AMC registration
 - Resources for enforcement
 - Clarification regarding consideration of professional designations
- Defeated bill that would have increased SBA appraisal threshold from \$250,000 to \$400,000
- IRS proposed rule on “qualified appraiser” cites AI designations as examples demonstrating competency
- SEC proposed rule on Asset Backed Securities cites “MAI Certified” appraisals versus non-MAI Certified appraisals
- Freddie Mac advances “best practice” that includes consideration of professional designations

Recent Initiatives

PROFESSIONAL PRACTICE CENTER

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» HOT TOPICS

Appraisal Institute Members: Click on an industry "hot topic" below to access a vast array of relevant information and resources.

[Members Only - Login Required]

» **NEW!** Liability Issues

» Appraisal Review

» Valuation of Contaminated Properties

» Appraising Energy Efficient Improvements in Residential/Commercial Properties

» Appraising in Declining Markets

» Appraising in Litigation

» Commercial Real Estate Workouts

YOUR PORTAL TO SUCCESS

The AI Professional Practice Center is a compilation of valuable resources and information covering the latest appraisal practices and procedures.

Professional Practice Documents

Commercial Appraisal Review Form & Compliance Checklist **[Members Only - Login Required]** 

Sample Agreements for Services **[Members Only - Login Required]** 

Sample Certification Statements **[Members Only - Login Required]** 

Use of Distressed Sales 

Standards of Professional Appraisal Practice 

Appraisal Institute Enforcement Procedures 

[View more . . .](#)

Regulatory Update



Ethics and Standards

Every member of the Appraisal Institute agrees to conduct his or her professional activities in accordance with the Code of Professional Ethics and Standards of Professional Appraisal Practice of the Appraisal Institute. In addition, the Appraisal Institute has developed a sophisticated peer review system through which it enforces its Code of Professional Ethics and Standards of Professional Appraisal Practice. Violations of the Code of Ethics or Standards can

Recent Initiatives

Guide Note

Development of an Opinion of Market Value in the Aftermath of a Disaster

MARKET VALUE

VALUATION CONSIDERATIONS
& PRINCIPLES

SUSTAINABILITY OF VALUE

COMPETENCY ISSUES

Recent Initiatives

Guide Note 5 Appraisals of Real Estate with Related Personal Property, Business Property or Intangible Assets



Recent Initiatives

MENU OF VALUATION SERVICES PERFORMED BY REAL ESTATE APPRAISERS ENHANCED EDITION

CRE Loan Renewal, Refinancing, and Other Subsequent Transactions

This Menu of Valuation Services is intended to assist commercial real estate lenders, including real estate credit risk officers and managers and similar persons (Chief Appraisers) in understanding the range of services that can be delivered by professional real estate appraisers. With \$3.5 trillion in commercial real estate debt outstanding, it is imperative for financial institutions to monitor collateral values as loan workouts, renewals and restructurings occur in accordance with agency regulations and guidelines. This menu describes the different options that can be delivered by real estate appraisers for regulatory compliance, portfolio and loan monitoring, and risk management purposes. The services will vary depending on the collateral position and agency requirements outlined in the *Interagency Appraisal and Evaluation Guidelines* and other policies such as the *Policy Statement on Prudent Commercial Real Estate Workouts*. Users of appraisal services are strongly encouraged to ensure regulatory compliance for any of the services outlined below.

VALUATIONS³

1. **Scope of work** options (appraisal development process) could be, but are not limited to:
 - a. Narrowed⁴. Ways to narrow scope may include:
 - i. “Update”⁵ (when there is a previous appraisal)
 - ii. No inspection (“desktop appraisal”)
 - iii. “Drive-by” inspection only
 - iv. Information about subject property taken from prior report and assumed to be accurate

¹As of January 2010

³When performed by an appraiser, USPAP applies. Valuations (appraisals, evaluations) of real property fall specifically under Standards 1 and 2.

Recent Lessons Learned

- Greed was pervasive
- Fraud was rampant
- You can't lend on credit alone – Collateral Matters
- At the same time
 - Loan Production was dominant
 - Appraisal departments were marginalized
 - Bank examiners had little expertise on appraisal matters and were largely ill-equipped and unprepared
- Appraisal is but one small piece of a larger machine
- Appraisal profession must remain steadfast in its professionalism and independence

Recent Clippings



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Former Bank of Clark County executive pleads guilty to concealing appraisals from regulators

By **Jeff Manning, The Oregonian**

February 19, 2010, 10:00PM

The wave of bank failures in the Pacific Northwest took an ugly twist Friday when a former high-ranking executive of the defunct **Bank of Clark County** pleaded guilty to concealing material facts from bank regulators.

Commercial real estate losses start hitting home

Nationally, banks could lose \$300 billion in downturn, report says

China cuts U.S. Treasury holdings

NEW YORK (Reuters) - China fell behind Japan to become the second-biggest holder of U.S. Treasuries in a sign the Chinese have been acting on recent complaints about U.S. policy by unloading U.S. debt.

Record number of US real estate loans overdue or in foreclosure, latest data shows

Recent Investigations



- Senate Government Affairs Committee Permanent Subcommittee on Investigations – *Wall Street & the Financial Crisis – Anatomy of a Financial Collapse*, April 13, 2011
 - “During the five-year period reviewed by the Subcommittee, from 2004 through 2008, OTS examiners identified over 500 serious deficiencies in Washington Mutual’s lending, risk management, and appraisal practices.”
 - “Still another area in which OTS failed to take appropriate enforcement action involves WaMu’s appraisal practices. OTS failed to act even after other government entities accused WaMu of systematically inflating property values to justify larger and more risky home loans.”
 - “WaMu’s decision to outsource the appraisal function received minimal attention from OTS.”
 - “Problems began almost immediately after WaMu outsourced the appraisal function.”

Recent Investigations



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- Financial Crimes Enforcement Network, Mortgage Loan Fraud Update, Jan 1, 2010-December 31, 2010 Filings
 - “In Q1, we addressed a new type of flipping scheme used in the context of short sales, termed “flopping” by industry and law enforcement. Flopping occurs when a distressed property is sold at an artificially low price to a straw buyer, who quickly sells the property at a higher price and pockets the difference. “
 - “During Q1, however, there were only two instances of flopping described in MLF SARs. **Over the course of 2010, MLF SAR references to flopping increased significantly, appearing in 112 SARs.** Based on FinCEN’s recent conversations with law enforcement partners, these statistics likely under-represent the occurrences of “flopping” schemes, because both law enforcement authorities and SAR filers are unfamiliar with the term. Use of related terms such as “short sale” and “broker price opinion” or “BPO” were stable throughout 2010. Flopping SARs typically described relatively recent activity, with suspicious activity start dates averaging one and a quarter years and end dates averaging seven months before being reported on a SAR.”

Recent Investigations



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- Treasury Office of Inspector General, Material Loss Review – IndyMac Bank (OIG-09-032), Feb 26, 2009
- OTS Identified Problems With IndyMac Appraisals in 2001 But Failed to Ensure the Problems Were Corrected
 - *“OTS identified problems with IndyMac appraisals early on. In its 2001 examination, OTS found that appraisals for the Home Builders Division (HBD) (1) violated policies and procedures, (2) violated OTS and Uniform Standards of Professional Appraisal Practice, (3) used inflated appraised values, (4) lacked market analysis and feasibility studies to support appraised value, (5) valued properties far in excess of the recent sale prices for the subject properties and (6) used retail values for subdivisions instead of prospective market value at the time of completion.”*

Recent Investigations

- *Cont...*
- *“OTS, however, did not report these issues in the ROE (Report of Examination)...In a limited examination later in the year, OTS followed up on the appraisal issues and concluded that additional attention was needed. However, while the appraisals did not meet standards, OTS concluded that existing appraisals and underwriting were sufficient to mitigate risk and did not issue an MBRA or other corrective action. The basis for OTS’s conclusion was not clear.”*

Recent Investigations



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- *Cont...*
- *“In its 2002 ROE, OTS examiners stated that IndyMac had hired a new chief commercial appraiser who reviewed loan appraisals. OTS examiners also stated that he was cooperative in working with the OTS to revise policies, discuss appraisal methodology and techniques, and work on acceptable resolutions of appraisal issues. However, OTS did not comment on his effectiveness.”*

Recent Investigations

- *Cont...*
- *“In its 2003 ROE, OTS reported that HBD appraisal policies, procedures, and practices were satisfactory and problem asset levels had declined. No specific comments were made about the efforts of the new chief commercial appraiser identified by OTS a year earlier. However, OTS reported concerns in the single family real estate appraisal function. OTS deemed this function satisfactory but said that improvements were needed.”*

Recent Investigations

- *Cont...*
- *“In its 2004 ROE OTS reported that IndyMac had effective residential and commercial appraisal functions, but recommended corrective actions to enhance controls associated with residential appraisals. We could not locate the supporting work paper documentation to determine what these actions were.*
- *In its 2005 ROE, OTS did not report on IndyMac’s appraisal function. We found that the examiner noted that in the prior year’s examination, OTS recommended improvements in the appraisal review and oversight function, and that both the OTS appraiser and examiner reviewed for corrective actions and found the recommendation had been implemented satisfactorily. No further details were provided in the work papers or the ROE.”*

Recent Investigations

- Cont...
- *“In its 2007 ROE, OTS identified serious issues with IndyMac’s appraisals. OTS found that the borrowers, rather than the mortgage originator, were paying the appraisers directly, which did not ensure appraiser independence. In several of the loan files, the OTS appraiser noted inadequate documentation. In the examiner workpapers, we noted that the examiner found appraisals where the property valuation was made without physical site inspection of the subject property or comparable properties, appraisals for which the appraiser was not located in the immediate area, appraisals where the valuations were based on public data sources, and appraisals in which no photos of the property or comparables were provided. Despite these serious weaknesses, OTS did not require action be taken.”*

Recent Investigations



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- *Cont...*
- *“In its 2008 examination of IndyMac, OTS found improvements in the appraisal function. OTS’s ROE stated that to improve credit quality, management implemented more stringent underwriting guidelines, tightened appraisal standards, and re-focused quality control efforts to high risk areas. However, we did not find that OTS’s examination workpapers supported these conclusions.”*

Recent Investigations

- *Cont...*
- *“This was puzzling to us because in 2008 we found that IndyMac hired a firm to conduct an assessment of its appraisals. The primary finding of the firm, based on interviews with retail and wholesale underwriters, was that IndyMac underwriting was not centrally managed and instead was handled in remote branches and in IndyMac’s Pasadena office. As a result, no consistency existed with appraisal underwriting. The firm recommended that policies and procedures be centralized and made consistent to ensure conformity to procedures. We did not see evidence of how OTS handled these findings and ensured IndyMac took the necessary corrective actions.”*

Recent Investigations

- *A recent internal review of Material Loss Reports conducted by the Appraisal Institute found:*
 - *In 2009, 64 percent of Material Loss Reports contained previous citations by bank regulators relating to appraisal management deficiencies*
 - *A review of 2010 Material Loss Reports, indicates 75 percent of failed banks were previously cited for appraisal management deficiencies*

FDIC Lawsuits

- On May 9, 2011, the FDIC filed a lawsuit in U.S. District Court (C.D. Cal.) against CoreLogic and various affiliated companies including CoreLogic Valuation Services, LLC, f/k/a eAppraiseIT, LLC ("eAppraiseIT").
 - In its complaint, the FDIC alleges that eAppraiseIT supplied potentially thousands of improper appraisals and that eAppraiseIT was grossly negligent in the provision of appraisal services in 2006 and 2007.
 - According to the complaint, the FDIC has sampled 259 appraisals out of the thousands at issue and alleges that 194 (or 75%) of them "contain multiple egregious violations of USPAP." Source: *Appraiser Law Blog*

FDIC Lawsuits

- The FDIC also sued LSI Appraisal, its parent corporation Lender Processing Services and various of their affiliates in the same U.S. District Court. This lawsuit also concerns appraisals delivered to or managed for WaMu during the same period.
 - In this lawsuit, the FDIC seeks approximately \$154 million in damages, but these alleged damages only relate to 220 specific appraisals or review appraisals supplied by LSI between June 2006 and May 2008 -- the FDIC says it has only sampled 292 so far (of course, the ones sampled would only be for loans that have defaulted).
 - The FDIC suggests in its complaint that there could be thousands more appraisals at issue. Indeed, the FDIC alleges that LSI supplied or managed more than 386,000 appraisals for WaMu during the relevant time period. Source: *Appraiser Law Blog*



112th Congress



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- Dynamics
 - Republican controlled House; Democrat controlled Senate; Democrat controlled White House
 - Deficit reduction = Congress is looking for revenue raisers and spending constraints
 - 2012 Elections around the corner
 - More gridlock likely



112th Congress

- H.R. 1755, Home Construction Lending Regulatory Improvement Act
 - Would require appraisers, lenders and examiners to use the —as-completed|| value when assessing loan collateral on projects that have reasonable prospects of reaching completion.
 - Would prohibit use of foreclosure and distressed sales as comparables.
 - AI – opposed as introduced



112th Congress

- Sensible Accounting to Value Energy “SAVE” Act (to be introduced)
 - Includes provisions supported by AI addressing competency and communication
 - Ensure delivery of building information (ratings, plans and specs) to appraisers whenever possible.
 - Would also elevate appraiser qualifications to require that any real property with energy efficiency features be appraised by a State Certified appraiser who has met higher
 - AI - Supports



112th Congress

- S. 339, Rural Heritage Conservation Extension Act
 - Amends the Internal Revenue Code to make permanent the tax deduction for charitable contributions by individuals and corporations of real property interests for conservation purposes.
 - A qualified appraisal by a qualified appraiser is required for the tax deduction
 - AI - Supports



112th Congress

- HR 1147, Community Recovery and Enhancement Act
 - CRE investment bill
 - If at least 80 percent of the invested capital is used to reduce outstanding commercial mortgage debt—with the remainder going toward capital improvement such as energy-efficiency enhancements and leasehold improvements to attract new tenants—new investment would qualify for the lesser of a one-time 50 percent or \$10 million bonus depreciation.
 - Fair market value is part of the maximum deduction calculation and a factor in determining eligibility for the deduction
 - AI - Supports

112th Congress

- HR 665, Excess Federal Building and Property Disposal Act
 - Requires the Director of the Office of Management and Budget (OMB) to: (1) conduct a Federal Real Property Disposal Pilot Program for the expedited disposal of real property that is not meeting federal government needs, and (2) identify criteria for identifying such property
 - Prohibits real property from being sold under the program: (1) for less than fair market value, (2) if it will not generate monetary proceeds to the federal government exceeding disposal costs, or (3) in a non-cash transaction.
 - AI – Supports Appraisal Provisions



112th Congress

- S. 1232, Amending ERISA
 - To modify the definition of fiduciary under the Employee Retirement Income Security Act of 1974 to exclude appraisers of employee stock ownership plans.
 - Bill, as introduced, does not include real estate appraisers
 - AI – Support with amendment



112th Congress

- H.R. 2056, Inspector General of the FDIC to Examine Impact of Bank Failures.
 - Study will look into the effect of loss-share agreements, the impact of consent orders and cease and desist orders, how the practice of using paper losses may have affected institutions, and other practices they use when dealing with troubled or failing institutions.
 - Calls for Inspector General to look into the implementation of the Interagency Guidelines.
 - Passed the House of Representatives.

112th Congress

- FY2012 Financial Services and General Government Appropriations bill
 - Provides funding for Financial Services and General Government programs and agencies.
 - Concerns on the drastically reduced levels of funding for the General Services Administration (GSA) Public Buildings Service. The House-passed bill eliminates funding for new construction and major renovations of Federal buildings
 - AI - Oppose-as passed by House of Representatives

Federal Regulations

- Going concern – SBA Standard Operating Procedure 50-10
 - Oct 1, 2010 policy requires 2nd business appraisal when component is more than 25 percent of the total
 - “Qualified Sources” definition includes CPAs, ASAs, ABVs, etc.
 - SBA has agreed to update policy, and AI has been working with the agency to recognize competent appraisers

Federal Regulations

- Interagency Appraisal and Evaluation Guidelines
 - As-is market value
 - Appraisal Review
 - Appraisal Independence
 - Going Concern
 - Evaluations
 - BPOs – do not satisfy definition
 - Appraisal, Evaluations, Collateral Monitoring

Federal Regulations

– Dodd-Frank Implementation

- Consumer Financial Protection Bureau
 - Interim Final Rule on Appraisal Independence
 - AMC fee disclosure
 - Non-bank examinations
- “Skin in the game” – review requirements & “qualified residential mortgage”
 - Appraisals required
 - Asset-backed Securities – Proposal recognizes “MAI Certified” appraisals

Federal Regulations

- DOL Fiduciary Responsibility
 - Proposed rule would define appraisers as “Fiduciaries”
 - “Investment advice
 - Fails to recognize diverse engagements of real estate appraisers by pension funds
 - Portfolio monitoring
 - Disposition
 - **“Independence Fiduciary”**
 - AI has engaged DOL in a productive dialogue

Federal Regulations

- IRS/SEC Regulations
 - Oversight and enforcement increasing
 - Circular 230
 - Valuation Misstatements
 - Letter 4477
 - Tax Court Opinions Mixed
 - Trust for Architectural Easements Enjoinment

Federal Regulations

- Financial Accounting Standards
 - FASB/IASB projects
 - “Lease Accounting” (Topic 840)
 - Investment Properties, IAS 40
 - Investment Companies
 - Fair Value and 3rd party subject matter experts

Federal Regulations

- Housing Programs
 - Future of Fannie & Freddie
 - Uniform Appraisal Dataset
 - Foreclosures, Modifications, rental housing program
- Multi-Family
 - AI to develop a “Primer” on affordable housing appraisals for use by state housing finance agencies, HUD, USDA, IRS
 - Recognized at White House event in July

Federal Regulations

- Bank Safety and Soundness
 - FDIC Appraisers supporting bank examinations
 - Faced immediate criticism by banks and some appraisers
 - Protocols will likely need to be developed

Industry Initiatives

- CRE Finance Council
 - CMBS 2.0
- CFA Institute
 - Global Investment Performance Standards (GIPS 2010)
- NCREIF/PREA
 - Real Estate Information Standards (REIS)

Looming Threats

- Rulemaking Processes
- Actors Seeking to “Rig” the Appraisal Processes
- Overreaction – Pendulum swinging too far
- Scope Creep
- Appraisal is a small layer in a large pond
- Part of an international machine
- Failure to Learn from Past Mistakes

Opportunities & Strengths



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- Assisting the Economic Recovery
- Resolving the Banking Crisis
- Valuation Issues at the Forefront
- Market Analysis
- Several Sectors Have Reaffirmed the Importance of Valuation
 - Pensions and Institutional Investors
 - CMBS 2.0
 - REITs
 - Financial Reporting – IFRS and GAAP
 - Banking
 - Non-banking, tax, litigation support, consulting
 - Forensic Valuation/Appraisal Review

Suggestions

- Talk with your clients!
- Work with clients who want your expertise and analysis!
- Diversify skill set and practice!
- Stay abreast and involved!
- Continue to do professional, solid work