



2600 Virginia Ave. N.W.
Suite 123
Washington, DC 20037
T 202-298-6449
F 202-298-5547
www.appraisalinstitute.org

Executive Vice President
John W. Ross
312-335-4110

Vice President,
Public Affairs
Donald E. Kelly
202-298-5583

Testimony of
Alan Eugene Hummel, SRA
President, Appraisal Institute
Chief Executive Officer, Iowa Residential Appraisal Company
Des Moines, Iowa

On Behalf of the
Appraisal Institute and
American Society of Appraisers

Before the House Committee on Veterans' Affairs
On

"H.R. 1500, the Veterans' Appraiser Choice Act of 2003"

Presented by
Alan Eugene Hummel, SRA
President, Appraisal Institute
Chief Executive Officer, Iowa Residential Appraisal Company
Des Moines, Iowa

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Mr. Chair and members of the Committee, I am Alan Eugene Hummel, President of Iowa Residential Appraisal Company in Des Moines, Iowa and 2003 President of the Appraisal Institute. I am pleased to be here today on behalf of the Appraisal Institute and American Society of Appraisers, which together represent more than 25,000 real estate appraisers in the United States, many of whom are active on the Department of Veterans Affairs (VA) Appraisal Panel.

We want to thank you for holding this hearing on H.R. 1500, the Veterans' Appraiser Choice Act, sponsored by Representative Adam Smith, Representative Lane Evans and Representative Michael Machaud.

According to the sponsors, veterans, realty agents and lenders have indicated concerns about the program, charging that the appraisal process is too slow. We disagree with such an assertion and, in fact, our research indicates just the opposite. Furthermore, we are concerned that the bill would jeopardize the independence of the appraiser and interject additional risk into the transaction at the expense of the veteran. While we appreciate the commitment of Rep. Adam Smith to improve the program, we cannot support the current legislation. To authorize those with a vested interest in the outcome of the transaction to select the appraiser is ill advised in our opinion and could lead to cases of improper client pressure or manipulation of the appraisal process. Inappropriate client pressure directed at appraisers has proven to be a contributing factor in many cases of mortgage fraud and predatory lending throughout the country. Many of your colleagues in the United State Congress have recognized this inappropriate pressure of appraisers as an issue that should be addressed. Congress should not assist in the proliferation of these practices, but unfortunately H.R. 1500 would do exactly that.

Although the VA appraisal program is not perfect, the changes proposed in H.R. 1500 do not make for a better program. In fact, if enacted, the result is likely to be longer turnaround times for appraisal assignments. Ultimately, H.R. 1500 could threaten what many of our members say is one of the "most honest housing programs in the federal housing repertoire." We recommend that Congress explore the recommendations outlined below and work to improve the effectiveness of the VA appraisal program without jeopardizing the independence of real estate appraisers.

The VA Appraisal Process and the Importance of Independence

The independence of the appraisal process is a fundamental principle that assures participants in a mortgage transaction that the value of a home held as collateral will reflect the market value. As you know, under the current Loan Guaranty program administered by the Department of Veterans Affairs real estate appraisers are selected by rotation from the VA Fee Panel, the "approved" appraiser list administered by VA.

Maintaining the independence of the appraiser is the key benefit of selecting appraisers by rotation and not by lenders, brokers, realty agents or prospective borrowers. The current rotational system is effective at providing for the independence of appraisers by having an unbiased party (the VA) select the appraiser on a rotating basis from an approved list of appraisers. By contrast, appraisers for conventional loans and Federal Housing Administration (FHA) guaranteed loans are chosen directly by lenders and mortgage brokers from a list of appraisers.

Overwhelmingly our members report that inappropriate pressure occurs in conventional and FHA assignment more frequently than in the VA appraisal assignments. The Appraisal Institute surveyed its membership regarding H.R. 1500. Eighty (80) percent of Appraisal Institute members who are approved on the VA Appraisal Panel say that the VA appraisal selection process is more effective at ensuring the independence of real estate appraisers than conventional or FHA appraisal assignments. Additionally, our members consistently report that instances of inappropriate client pressure have increased since the Department of Housing and Urban Development allowed lenders in 1994 to select appraisers, and that this pressure is far more likely to occur in the FHA program than in the current VA program. Many members of our organizations have become so frustrated with the increased pressure resulting from the FHA appraisal process, that they have removed themselves from the FHA Appraiser Roster entirely.

Appraisal Institute members also expressed concern about the impact H.R. 1500 would have on inappropriate client pressure of appraisers. Eighty-eight (88) percent said that instances of inappropriate client pressure would increase if the VA appraisal selection process is changed to allow veterans to choose the appraiser.

Simply put, the reason inappropriate client pressure exists is because the amount of the loan approved by VA is dependent upon the value of the house, and the value of the house is determined by the appraisal. In conventional and FHA loans appraisal clients control the workflow to the appraisers and thereby are in a position of influence over the appraiser. As in any business relationship, there are normal pressures, influences and resistance exerted by all parties in the transaction. A broker might ask an appraiser if a certain comparable sale was used in their appraisal report, or a loan officer might ask if too much of an adjustment was applied by the appraiser in the appraisal report. These are legitimate questions that do and should occur between a client and an appraiser.

However, legitimate inquiries by clients cross the line when a predetermined value is required of an appraiser, or when future work for the appraiser is contingent upon meeting this predetermined value being met. Frequently, our members confront cases where productive dialogue between clients devolves into blackballing, threats and other coercive tactics. The problem has become so prevalent in conventional assignments that Rep. Janice Schakowsky has introduced legislation in the past three sessions of Congress that would prohibit inappropriate pressure of appraisers. Although Congress has not considered this legislation, it has shed light on the issue. Congress should be concerned about this, since many of the predatory lending and mortgage fraud schemes that have been uncovered recently were caused by inappropriate client pressure.

Borrowers Should Not Choose Appraisers

We recognize the intent behind the idea of having veterans choose the appraisers is to create a degree of market accountability for appraisers on the VA Appraisal Panel. Apparently, lenders, brokers and realty agents have perceived VA appraisers as being “unaccountable” – and in some instances there may be

some truth to this. However, the proposals outlined in H.R. 1500 would needlessly grant greater control over appraisers by lenders, brokers and realty agents, and worse, would use veterans as the conduit for exerting such pressure.

For borrowers, veterans or otherwise, to dictate to the VA the use of a specific service provider is problematic. Such a practice injects into the selection process a party with a vested stake in the outcome of the loan. As many active duty veterans move to new areas after assignments or retirement and may not be familiar with local market conditions, such a process would leave them vulnerable to unscrupulous players in the real estate market. If passed, H.R. 1500 could have a profound effect as predatory lenders, brokers and realty agents will likely “suggest” veterans choose favored appraisers.

We need not look any further than the 1980s to see why Congress should avoid creating moral hazards between borrowers, lenders and appraisers. A major contributing factor to the savings and loan crisis was relationships between borrowers and appraisers, which later caused Congress to require licensing and certification of real estate appraisers, in addition to specifically prohibiting borrowers from ordering appraisals.

H.R. 1500 would also add to the misperception that appraisals are done on behalf of borrowers. Although the independent function of the real estate appraiser protects both the lender and the buyer, ultimately, the client of the appraiser is the Department of Veterans Affairs, not the borrower or lender. We have long recommended that if a borrower is concerned about the value of the home being purchased, a second appraisal ordered by the buyer could satisfy their concern.

Finally, we believe H.R. 1500 would actually slow down the appraisal process, which is contrary to the goals of the legislation. As we understand it, if the bill is enacted each veteran will be given a notice of their right to choose the appraiser or to opt out of the process and have VA assign the appraiser on a rotational basis. If the veteran elects to choose the appraiser, it is unclear as to how they would go about this, which raises many questions:

- Would the veteran have to choose immediately?
- Would the veteran be given a certain number of days to select the appraiser?
- Who would provide the veteran with the approved list of appraisers?
- On what basis would veterans make the selection: the advice of the realty agent, lender or mortgage broker?

What should be done instead?

Given that H.R. 1500 would not improve the current system, we offer the following suggestions for the Committee to consider. Each recommendation would preserve the independence of the real estate appraiser and improve the effectiveness of the program.

1. Conduct an objective assessment of the effectiveness of the VA appraisal program

We understand H.R. 1500 was introduced because of complaints from mortgage brokers, realty agents and lenders about the timeliness of the VA appraisal assignments. Some organizations have contended VA appraisals are the slowest to be performed of any type of mortgage transaction.

Market research says otherwise. Eighty-eight (88) percent of Appraisal Institute members on the VA Fee Panel say that the turn-around time for VA assignments is not longer than conventional assignments. Eighty-six (86) percent say the VA turn-around time is not slower than for FHA appraisal assignments.

VA's stated timeliness requirement for fee appraisers is that they submit their report in the same amount of time as conventional appraisals performed in the area. Currently, ninety percent of appraisals performed are reviewed under the Lender Appraisal Processing Program (LAPP). Under LAPP, the lender's designated Staff Appraisal Reviewer (SAR) reviews the appraisal and is required to analyze the timeliness of the submission by the appraiser. In those cases where they identify unacceptable timeliness, they are instructed to notify VA so that VA may take appropriate action. The VA reports that it is rare for lenders to report timeliness issues.

In addition, the VA is undertaking several e-commerce initiatives requiring VA appraisers to have email and complete VA appraisals electronically. Our organizations support these initiatives and their impact should be reviewed.

Further, slow turnaround time for an appraisal may not be the result of poor appraiser performance. It is common for a lender to not request the appraisal assignment for several days or even weeks after receiving a loan application. In addition, in some cases, an appraiser can find it difficult to gain access to the property, which can add several days to the completion date. These factors, of course, do not reflect the competency of the VA appraiser.

Given the disagreement over whether VA appraisals are slower than market averages, we recommend Congress call on an objective party such as the General Accounting Office to conduct an investigation into the effectiveness and timeliness of VA appraisal assignments. Such an investigation could compare the VA program to the appraisals performed in the conventional and FHA markets.

2. Allow for Current VA Reforms to be Fully Implemented

In 2002 and 2003, VA undertook several programmatic initiatives in response to recent complaints about its appraisal program. For instance, a series of complaints in the Norfolk, Virginia (Tidewater) area resulted in a change in appraisal ordering procedures. Ironically, the procedural changes made in the Tidewater region were approved by many of the organizations now calling for the upheaval of the VA appraisal program.

The new procedures are known as the "Tidewater Experiment." The process, which was developed through meetings with stakeholders in the Tidewater region, requires appraisers to notify a lender designated point-of-contact when it appears the appraised value will come in below the sales price. Once the appraiser notifies the lender and agents of the differential between the appraisal and sales price, the point-of-contact has two working days to provide additional information to the appraiser in a format similar to a comparable sales grid on an appraisal report. After receipt of additional information, the appraiser is required to complete the appraisal report. If the information provided to the appraiser does not result in an increase in value, the appraiser will report on the addendum the following information: who provided the additional information; what information was provided; and why it did not change the opinion of value.

We have had discussions with the VA about the Tidewater Experiment, and we understand the Department has received positive comments about the program. The program has apparently been so successful in resolving disputes and aiding timeliness that the VA has drafted plans to expand the program in other areas of the country. It should be noted, these plans were drafted prior to H.R. 1500 being introduced.

Given the positive results of the Tidewater Experiment, and the VA's plans to expand the program nationally, we recommend VA be given sufficient time for this program to be implemented. If the program is as successful as it appears, we recommend it be implemented throughout the country.

3. Increase the Size of the Appraisal Panel

If the turnaround time to complete VA approved-appraisers is longer than local market expectations, the problem may be that there are not enough approved appraisers on the VA panel. This has been a historical complaint about the VA Appraiser Panel, going back since the program was first implemented.

There are many qualified residential real estate appraisers, including many in our organizations who are interested in applying for acceptance on the panel. The Appraisal Institute surveyed its members who are currently not active on the VA Appraisal Panel, and 47 percent say they are interested in applying for acceptance on the VA Appraisal Panel. When asked how many appraisal assignments they would need to perform per month to make it worth their while to apply to the VA Appraisal Panel, 58 percent it would take 1-10 appraisal assignments per month. These figures are significant given the Appraisal Institute's diverse membership, which consists of residential and commercial appraisers. It is clear that many qualified and experienced appraisers would like to participate in the VA appraisal program.

Currently, there are approximately 4,800 appraisers on the VA appraisal panel. We recommend VA expand the size of the panel, particularly in areas where lack of timeliness has been demonstrated and verified as not meeting conventional standards.

4. Require Periodic Recertification of VA Appraisers

The VA currently requires appraisers to meet state licensing or certification requirements, which contain minimum continuing education requires. The VA also requires VA appraisers to attend annual VA meetings once a year.

Our members on the VA Appraiser Panel would support recertification to the VA Appraisal Panel. When surveyed about whether they would be willing to undergo periodic recertification to maintain their status on the VA Appraisal Panel, 88 percent responded "Yes."

The VA could require regular recertification of all VA appraisers, or VA could bolster their annual meetings with VA appraisers to present and conduct agency-specific information and training. Strong recertification requirements and/or stronger agency specific training requirements could increase VA appraiser professional development.

5. VA Should Actively Discipline Poor-Performing Appraisers

Our members resoundingly support disciplining poor performance by appraisers. We believe poorly performing appraisers should be appropriately disciplined if their performance warrants disciplinary action and removed from the VA Appraisal Panel if necessary.

The VA has not been overly aggressive in disciplining VA appraisers, who may be culprits for some of the experiences of veterans, lenders, and realty agents. As we understand it, 12 VA appraisers were removed from the VA Appraisal Panel in 2002 for disciplinary reasons, while 163 VA appraisers resigned their membership. We understand many of resigned appraisers may have had their active status removed had they not resigned their status on the Panel.

The VA could establish a more active appraiser complaint resolution system, perhaps creating more concrete stages of discipline. If the VA embarks on such a program, the system should be fair to the appraiser and allow the appraiser an opportunity to refute claims made against them. If a minor offense has been found, VA should sanction or discipline the appraiser accordingly.

Concluding Comments

As the largest professional organizations of real estate appraisers in the United States, we are concerned about the criticisms expounded about the VA appraisal program. The independence of real estate appraisers is essential to maintaining a sound and effective loan guarantee program. Unfortunately, H.R. 1500 would jeopardize the independence of real estate appraisers. We urge Committee members to explore the recommendations outlined above before advancing H.R. 1500. The VA appraisal program can and should be improved, but we encourage Congress to do so without jeopardizing the independence of real estate appraisers.

About the Appraisal Institute and American Society of Appraisers

The Appraisal Institute is the acknowledged worldwide leader in residential and commercial real estate appraisal education, research, publishing and professional membership designation programs. Its extensive curriculum of courses and specialty seminars provides a well-rounded education in valuation methodology for both the novice and seasoned practitioner. Members of the Appraisal Institute form a network of highly qualified professionals throughout the United States and abroad. They are identified by their experience in and knowledge of real estate valuation and by their adherence to a strictly enforced *Code of Professional Ethics and Standards of Professional Appraisal Practice*.

The American Society of Appraisers is an organization of appraisal professionals and others interested in the appraisal profession. International in structure, it is self-supporting and independent. The American Society of Appraisers is the oldest and only major appraisal organization representing all of the disciplines of appraisal specialists, including real property. ASA is diligent in its efforts to strengthen and uphold the *Principles of Appraisal Practice and Code of Ethics* in order to protect the client.

We appreciate this opportunity to provide our official comments for the record. Should you have any questions, please contact Don Kelly, Vice President of Public Affairs, Appraisal Institute at 202-298-5583, dkelly@appraisalinstitute.org or Ted Baker, Executive Vice President, American Society of Appraisers at 703-733-2109, tbaker@appraisers.org.