Federal Housing Finance Agency,
Office of Housing and Regulatory Policy,
400 7th Street SW, 9th floor,
Washington, D.C., 20219.

This is a response to the Request for Information on Appraisal-Related Policies (RFI) dated December 28, 2020.

Below are my short answers to the questions posed. Following these short answers is a longer answer section that provides more detail and solutions to these questions.

<u>Short Answers</u>

A1.1
There is no need for new valuation solutions. While there are areas with a “shortage” of appraisers, most of the shortages and problems lenders are facing are self-inflicted; the solutions many lenders and appraisal management companies (AMC) are proposing will reduce the quality and accuracy of appraisal and introduce new problems into the collateral system. **Every** new process or system will experience an increased failure rate producing unforeseen consequences; the same is true for what is being proposed.

Additional high-quality training will always assist in producing better appraisers and appraisals.

Further explanations and solutions regarding the proposed “solutions” are detailed at the end of the Short Answers Section of my report.

A1.2
The risks posed by the use of non-traditional valuation services far out-weigh the problems and failures that will develop if implemented. In most instance where I have been initially involved or reviewed the work where an appraiser was **not** the person inspecting the subject property, descriptions of the neighborhood, comparables, and subject contained significant errors. The value conclusions in the associated appraisals were inflated, in some instance by more than 100% above the property’s true market value. As an example. A “property inspector,” who was not the appraiser, something I didn’t know until the end of the inspection, inspected a property that I own. Due to the size and complexity of the property I spent more than an hour helping the “assumed appraiser” understand the property and specifically pointed out several of the problems with the property. Later, when I read the appraisal, performed by a non-inspecting appraiser, many of the problems with the property were not outlined; and despite numerous photographs, many of the issues, including encroachments, and ownership issues, were not mentioned. The result was an appraised value many times higher than reality. When these issues were pointed out to the lender, I was told that “it didn’t matter and would not impact the loan.” If the appraisal didn’t matter, then why was it ordered in the first place? More importantly the lender paid for a meaningless document.

Further explanations and solutions regarding a bifurcated appraisal process are detailed at the end of the Short Answers Section.

A1.3
Yes, appraisal waivers have a place within the Enterprises policies; the most efficient use would be where there has been a recent appraisal, by a qualified appraiser and the Enterprises are aware of no major issues impacting the local marketplace. However, even with a limited time window there may have been physical changes to a property, or adjacent property, that would negatively impact its value. In several instances I have inspected a home, recently purchased, and discovered that the new owners were in the middle of making substantial changes to the house. At the time of my inspections the homes were unlivable and would not qualify for a "typical" 30-year mortgage. In another instance there had been extensive damage due to a storm and flooding. If a lender had refinanced any of these homes, the valuation would have been based on incorrect information resulting in loans that would have exceeded the property's value. If waivers are used, I would suggest that they are limited to A) no additional extension of credit, B) limited to no more than one year after a prior full inspection appraisal, C) instances where the loan to value ratio was less than 60% of the property's value (based on the older appraisal), D) at a minimum, a drive-by inspection be performed by someone, and E) a cap be implemented on their use which would force the Enterprises to use this process as a limited option rather than becoming a standard of operation (based on a total % of all refinance loans).

Further explanations and solutions regarding a bifurcated appraisal process are detailed at the end of the Short Answers Section.

A1.4
While it may help with addressing appraiser capacity it will result in decreased accuracy and reliability of the final appraisal. Based upon the experiments we have run using third-party inspectors the resulting appraisal reports are gravely flawed. The risks of using a third-party inspector is the lack of responsibility for their actions and reports they produce; couple this with the low fees they are being paid in the various experiments being tested and you have the components leading to failure. Several other countries have utilized the bifurcated appraisal process and in the reports I've read, both parties (inspector and appraiser) blame the other party **when** there is inaccurate information and value conclusions. Both parties complain about the low fees and the pressure they experience to produce more inspections or appraisals per day. If I were a client receiving seriously flawed appraisal reports, created via the bifurcated process, I would sue both parties for their negligence. The problem is… the inspector isn't licensed, has no overriding legal obligation to the lender, borrower or the Enterprises and would be impossible to sue if they provided incorrect personal information and/or fled the state.

Please read my longer answer to this question at the end of this document which lays out simple solutions to the "appraiser shortage" dilemma.

A1.5
At this time, there isn't a need for additional policies; what is needed is for the Enterprises to enforce the laws, rules, and guidelines that are currently enacted. It is a failure on the part of numerous lenders, Fannie Mae, Freddie Mac, and the Federal Housing Finance Agency to allow the use of sub-par appraisers and their tolerance for non-compliant appraisals that pose the greatest risk.

For a more detailed answer please see the article at the end of this section.

A1.6
Only an older demonstration version of the updated form has been widely distributed, therefore whether the new form meets, or fails to meet, the needs of the industry is not fully known. By failing to include input from more appraisers, the industry is missing an opportunity to learn from the primary users of the new form and provide education regarding the GSE's current appraisal requirements.

B2.1
Many appraisers are asking the Enterprises to provide them with information related to the market or adjustments that should be made between the subject and a comparable. They are looking for information that will help them get their appraisals through a "review" by the collateral underwriter. **However**, it is up to the local, geographically competent appraisers to determine these components and information and not rely upon information from the Enterprises. Therefore, other than education, the Enterprises should limit the information that they provide to appraisers.

The Enterprises should provide more correction letters to appraisers that fail to properly fulfill their appraisal requirements. Warning letters have great impact on appraisers by informing the appraiser of the information and quality of work expected, that their work is being reviewed, sub-par work will not be acceptable, and how to correct failures. Warning letters can be considered the "stick" in a carrot and stick methodology which should be employed to a far greater extent than is currently employed.

While the Collateral Underwriter and the Enterprises have indicate there is a low failure rate for appraisals, in the reports we have audited, after being "reviewed" by the collateral underwriter, we find a much greater failure rate (USPAP and factual) than is being publicly reported.

The Enterprises should offer more education regarding common appraisal failures, Guideline requirements, and specific information related to the scope of work required when providing appraisals for lenders and the GSEs. I teach appraisal classes all across the USA and the poor level of education that was provided to appraisers, by their mentors and, provided by some of the larger schools leads to extensive misunderstandings and failed appraisals. Greater outreach by the GSEs would be a low-cost method to improving the quality of appraisals.

B2.2
Training. Lenders often rely on third parties or poorly trained internal staff when utilizing existing collateral tools. Due to low fees and extensive pressures, staff often has a high turnover rate, have not been properly trained and as a result the tools are not being fully utilized allowing poor quality appraisals to be accepted. Better training via more web-based systems would aid in this segment.

B2.3
No recommendations.

B2.4
A clearer and simpler check list outlining the requirements for issuing a waiver would result in fewer attempts at manipulation. Better education regarding the requirements, as well as when a waiver is granted, or denied, would be of assistance to lenders, consumers, and appraisers. A central list, known to all lenders and maintained by both Enterprises, tracking when a waiver is requested, denied, and accepted can help minimize the attempted manipulation. The Enterprises can also use this information to identify higher risk lenders which are attempting to manipulate the waiver system.

B2.5
There is no enforcement mechanism available today, covering third-party inspectors. There is no viable system that would properly protect the Enterprises, appraisers, or consumers. Any third-party, if found to be failing in their duties, can simply change their name, state in which they work and/or, shift to a different user. Any enforcement process would require changing laws, setting up departments, creating written requirements and result in increased costs for little return. Any system would require approval in each state and likely take 10 years to fully implement. A new layer of bureaucracy will be needed which will increase costs, likely with little return or improvement in the availability of appraisers or the quality of their work.

The enforcement system in operation today is the state licensing/certification of appraisers and their requirement to follow the Uniform Standards of Professional Appraisal Practice (USPAP). It would be far easier to bring more appraisers into the existing system where current enforcement actions by states and the Enterprises could, and should be, utilized to a much greater extent.

B2.6
See the answer posted in Question A1.3 and the longer article at the end of this section.

B2.7
Yes, the COVID-19 flexibilities should be more properly refined through the use of alternative forms instead of altering existing forms. The use of the same form, but with different scopes of work creates confusion among the appraisers as well as the entities that use or read appraisal reports. Different forms, each with different scopes of work would help everybody. Clearer protocols should become part of the Guidelines and readied for use in the future when additional “disasters” arise. Plan and educate now for likely recurring problems in the future.

C1.1
There are simpler and easier process, than what’s being considered now, that can aid the appraisal industry. There is no need to implement many of the processes that lenders, Fannie Mae, and technology companies are suggesting are the “solution to the appraiser problems.” Improving the existing process, better education and enforcement is a much quicker, simpler and lower cost method that would benefit all.

For a more detailed answer please see the article at the end of this section.

C1.2

Based on the thousands of appraisers I interact with, there will always be a group of appraisers that will not adapt to change while other, younger appraisers may attempt to adapt - begrudgingly. The implementation of the UAD and Collateral Underwriter forced many low-quality and high-quality appraisers to quit the business, the same will happen if a bifurcated appraisal process is utilized. As an example, in a small town in Eastern Washington out of 35 appraisers in the area, after implementation of the UAD, ten of them "retired" or shifted into a different business; they did not want to deal with the additional education and costs (software, Internet access & software). Even the upcoming change in the "form" will trigger an exodus of **some** appraisers. For numerous highly competent appraisers the requirement of a computerized "review master" along with its ridged data requirements coupled with the UAD implementation forcing appraisals to meet a computer's requirement for information (even when wrong) triggered many of these people to stop appraising for lenders. On a daily basis I communicate with appraisers, some of which were past chief appraisers for banks, our topic of discussion often includes comments of ***"how happy they are since they left bank appraisals behind and switched to providing work for other clients"*** (usually legal cases). The rigidity of using only UAD abbreviations, certain address formats, and descriptions that are necessary for the "UAD computer" to understand the appraisal information (coupled with the low fees offered by AMCs) has led many of these top tier appraisers to avoid working for lenders. The proposed implementation of the bifurcated appraisal process will trigger additional exits from the lending world (another self-inflected problem).

The new forms will require appraisers to obtain additional education and time to become accustom to the new input, formats, and high speed-always on, connection with the Internet. This will result in new software and higher costs for appraisers, especially in rural and outlying areas (exactly the places lenders need more appraisers). Again, due to the quest by lenders to obtain appraisals at the lowest cost, many appraisers will not be willing to pay the price just to make a lender's life easier. And the statements by many, including Fannie Mae, various lenders, and AMCs feed appraisers that ***"The appraiser no longer has to travel to view the subject or comparables therefore they can produce more appraisals every day"*** rings hollow and untrue. This new proposed system wasn't requested by appraisers, it was requested by the lending industry the very ones that desire and strive to obtain appraisals quicker and cheaper by shot-gunning orders out to dozens of appraisers in a quest to obtain the cheapest appraisal…..not the best. They are driving the quest for lower cost appraisal and collateral systems. If lenders and AMCs paid appraisers more, the perceived shortage of appraisers would cease.

C1.3

No. A change in appraisal policy or processes isn't the solution, more appraisers being able to make a living would help all. Please read the articles attached at the end of this section.

C1.4

There is always some level of discrimination usually by the less educated however, I've only observed discrimination by two appraisers, out of thousands. A properly implemented appraisal provided by a competent appraiser uses the sales that exist in the subject's neighborhood. Appraisers should not use sales from outside a neighborhood, when more similar and closer sales exist. Market value is based on data from the neighborhood. The outlandish suggestion, by some who are blaming discrimination for lower appraised values, fail to understand the requirement for using nearby sales to properly value a

home. Often what these people are claiming is "discrimination" is simply the implementation of proper appraisal methodology which they do not understanding.

For purchase transactions, other than the borrower's name, the appraiser does not know who the buyer is or what that person looks like. If the buyer/borrower is unknown, the opportunity for discrimination does not exist.

C1.5
Appraisers being properly trained to more accurately describe market areas, neighborhoods, and properties coupled with making properly supported adjustments for differences produces more accurate value conclusions in all neighborhoods. Educating appraisers regarding the use of non-descriptive words such as "pride of ownership" and the need for more data driven descriptions can help produce superior appraisers with fewer problems. The collateral underwriter coupled with a competent reviewer should be able to spot appraisals that are anomalies in any area.

C1.6
See the following information and expanded explanations.

<u>Further Detailed Explanations Regarding The Above Questions</u>

Several of the questions asked within the FHFA's RFI are interrelated and may be answered with a response focusing on the availability of appraisers and enforcement of appraisal quality.

Clearly some areas of the United States are experiencing a shortage of appraisers, the shortages are often in rural or small-town areas. However, in most areas the "shortage" of appraisers is directly to the process lenders and AMCs employ when attempting to hire appraisers in other words they are self-inflected and created by the lending industry. Daily I receive appraisal requests where the Lender/AMC is offering a fee that is half of what we receive from quality lenders. These "sub-fee" lenders then complain about a "shortage"; **there isn't a shortage of appraisers, there's a shortage of appraisers willing to work for low fees.** Their solution is to create a unique twisted process to solve their problem of locating appraisers who will work for the low fees that existed 15 years ago.

In our capitalist society, any shortage of a commodity, product, or service is best cured through the basic process of supply and demand. A shortage of appraisers can be simply alleviated by increasing the fees paid directly to appraisers. There is no need to introduce new more complex appraisal processes or additional parties (via a bifurcation of the appraisal). Many of these questions and suggestions listed in the RFI will introduce more problems, risks, and failures, many of which will remain unseen until the failures appear in the future, as they did in 2006-2011. The bifurcation of an appraisal process will in no way increase the quality of appraisals or their reliability.

At the end of this letter I've attached an article describing the issues encountered when attempting to perform bifurcated appraisals.

Supply/Demand
Over the past 10 years the price paid by lenders (and passed on to consumers) for appraisals has increased dramatically. However, these increased costs have not been paid to the appraiser; they have been siphoned off by a third-party, an appraisal management company (AMC). The AMCs have taken over a job that **was** handled internally by a special department within a lender's organization. Federal laws prohibited lenders from marking up the cost of an appraisal to fund their internal appraisal departments. However, there is no such prohibition if a company outside the bank provides the same appraisal management service, even if partially owned by a lender. As a result, the management of most appraisers has shifted outside the lender's organization, reducing a lender's operational costs. AMCs, for the most part, **charge lenders zero for this service.** AMCs require the appraiser to pay for their "management" by taking up to a 60% portion of the "appraisal fee"; this has resulted in appraisers being paid 40-60% less than they were paid years ago, prior to the widespread use of AMCs. Appraisers didn't ask to be "managed" by a third-party however they are the ones forced to pay for it. The dynamics of supply/demand have been thrown off by the introduction of a new process and third-party….the AMC. It is the reduction of the fee paid to appraisers that is the underlying cause of the idea that there is an appraiser shortage. In an effort to profit from the management of appraisers, numerous mortgage brokers, mortgage lenders and financial institutions have acquired ownership of the AMCs (thus side-stepping the prohibition of marking up appraisal fees within an institution). They have syphoned off a portion of the fees paid for an appraisal and now demand a cheaper way to acquire appraisals – a self-inflected wound.

When consumers view their loan disbursement document, they see a line for the appraisal fee, they do not understand that this is **not** the fee the appraiser receives (therefore it's misleading).

In the past, appraisal firms were responsible for hiring, training, and paying appraisers; the appraisal fee was sufficient to pay for the training of new appraisers. Due to the syphoning off of fees, there is little incentive for an appraiser to take on the responsibility of a trainee, again slowing the introduction of new appraisers into this system. As the owner of an appraisal firm, I have not hired a trainee in the past 15 years. However, as of late 2020, appraisal fees had finally risen, to a point, where it makes economic sense to begin hiring trainees.

When people factor in the low pay coupled with the time it takes to obtain a certificate and become proficient in the appraisal world, it becomes difficult to convince a college student that appraising is a viable career choice; again restricting the introduction of new appraisers into our system.

The various processes promoted by the lending world and queried in the RFI would not increase the fee paid to an appraiser it is designed to further **reduce the fees paid by lenders.**

The solution to this syphoning off the appraisal fee is to **a)** require the lender to pay for the management of the appraiser, not the appraiser and **b)** increase the fees paid directly to the appraiser. Increasing the fee paid to the appraiser will allow supply/demand to rebalance itself and the perceived "shortage" of appraisers will eventually go away.

Quality and Enforcement
For the majority of appraisals we review, the quality is terrible. Many lack adequate or accurate information regarding the neighborhood, market demand, quality or condition of the subject and wild guesses are made regarding how the market adjusts for differences. It seems that the majority of appraisers adjust at a rate of $25.00 for each square foot of difference between the subject and a comparable regardless of a home's location or value. In February 2015 FNMA sent out a letter indicating that appraisers were failing to make proper adjustments for differences in a home's square footage.[1] The study covered more than 700,000 appraisals nationwide. FNMA has a list of every appraiser who applied incorrect adjustments and yet very few of them ever received a warning letter notifying them that their appraisal methodologies were inaccurate. In other words, FNMA has, and continues to, tolerate poor appraisal quality. Due to their silence and lack of "gray" or "black-listing" appraisers, poor appraisal performance is not only tolerated it appears to be encouraged; this is a disservice to the appraisers who are trying to provide high quality work and the people who rely on their reports. Allowing a bifurcated appraisal process will do nothing to improve the quality of appraisals it will, without a doubt, reduce the quality.

Another problem involves the failure of appraisers to personally drive-by each of the comparables and taking **original** photographs (a basic requirement for FNMA, FHLMaC, VA, FHA, and most lenders (1004-forms)). Instead of using the required **original** photographs many appraisers illegally use copyrighted photographs from their local multiple listing system (MLS), place them into an appraisal, then CERTIFY that the photographs were personally taken by the appraiser. Once this misleading information is placed in an appraisal it is used to mislead lending institutions as well as the GSEs regarding the scope of work actually performed. When an appraiser fails to personally inspect a comparable, they often are not aware of many critical factors that can impact a property. The point of viewing a comparable is to assist in **comparing** the subject to another property and its surroundings. Without an actual viewing of the properties, this comparison process is compromised, thus reducing the reliability of the appraised value.

Fannie Mae and Freddie Mac, through their "collateral underwriter systems" acquire more than 100,000 exterior photographs of properties each day.[2] Their collateral underwriter system can recognize when an appraiser has failed to personally inspect a comparable property. As an example, in Prescott Arizona the same photograph of a property has been used in at least ten different appraisals supplied by five different appraisers. In each case the photograph used by these appraisers is an exact match with the photograph supplied by the local MLS (including the MLS trademark). This is not an isolated instance. In the vast majority of appraisals in many different areas we see photographs, supplied by the local MLS, being used repeatedly by numerous appraisers; often the very same people who brag about how many appraisals they perform each week. These same appraisers certify that they have viewed a comparable and personally taken the photographs – they are misleading…. lying… to the lenders and GSEs.

Between January of 2014 through March of 2017 Fannie Mae sent out 3,500 warning letters to appraisers making them aware of their failures (involving a multitude of issues). 3,500 letters work out to be three warning letters a day. Considering the collateral underwriter "reviews" upwards of 20,000

[1] Lender Letter LL-2015-02
[2] 20,000 appraisals a day x 5 exterior photographs per appraisal = 100,000 photographs x 280 days a year = 28,000,000 photographs per year entered into FNMA's collateral underwriter system.

appraisals each day, three warning letters a day indicates that the GSEs are missing golden opportunities to inform and improve the quality of appraisals.

“Black-Listing” Appraisers

The GSEs have a list of appraisers whose work should no longer be acceptable for submission as part of a loan package. Numerous states have extensive lists of appraisers who have been disciplined, sometimes for including fraudulent information on their appraisal reports; some of these appraisers have had their licenses revoked. However, the GSE’s list does not make use of the information provided by fifty states. I’m aware of several appraisers who, prior to having their license revoked in one state, canceled their license then applied for and received a new license in a different state. Fannie Mae’s list does not appear to contain the names of the appraisers who have received severe disciplinary actions by a state. If a severe disciplinary action or revoked-licenses is **insufficient** to warrant inclusion on Fannie Mae’s “black-list,” what does?

I had an appraiser in Phoenix brag about how he is personally and individually producing twenty+ (1004) appraisals a week all without serious concerns being raised by the lenders who are selling these loans to the GSEs. Based on a quick reading of one of his appraisals it was obvious that the work was fraudulent - and still he pumps them out week after week with no negative ramifications.

These are just a few of the many appraisal failures that are being tolerated by lenders that sell their loans to the GSEs. Due to this tolerance appraisers who can produce a dozen appraisals a week are better compensated than appraisers who strive to provide superior work and help protect the lending system. This is another reason many appraisers are disillusioned and will not bring new appraisers into this system.

Reporting of Suspicious Activity

Overt erroneous appraisal information is an attempt to mislead lending institutions including institutions under the supervision of the Federal Housing Finance Agency (FHFA). By federal law, when any lender, Fannie Mae, or Freddie Mac become aware of attempts to mislead a financial institution a Suspicious Activity Report (SAR) **must** be filed with FinCEN.[3] Commencing in May, 2014 the government sponsored entities had new reporting requirements placed on them; they **must** report **all** suspicious activities and **all** attempts at misleading a lending institution.[4] However, between August of 2014 and December 31, 2019 the GSEs filed fewer than 200 SARS concerning appraisals.[5]

Many of the appraisals we review contain misleading information including false descriptions of the subject property, failures to describe adverse conditions, failures to inspect and photograph comparables, failures to describe the money laundering schemes being attempted by the buyer and seller (inflating purchase prices and flowing cash directly to the buyer to be used for the buyer’s down payment), inclusion of personal property such as a car in the purchase, financed by a mortgage. The result of these failures produces inflated appraised values, however the GSEs have only reported 200 SARs in a 64-month period. This low reporting rate is shameful and indicative of lenders and the GSEs

[3] Currency and Foreign Transactions Reporting Act of 1970 (commonly referred to as the "Bank Secrecy Act" or "BSA") 31 U.S.C. 5311-5314; 5316-5330; 533; 5332; 12 U.S.C. 1829

[4] Federal Register Volume 76, Issue 216 (November 8, 2011); B. FinCEN’s Anti-Mortgage Fraud Initiatives

[5] FinCEN Suspicious Activity Report; filings by type of suspicious activity by Housing GSE

tolerance of poor work. The GSEs have failed to fulfill their federally mandated requirements despite the fact that the Treasury Department and FinCEN have the ability to impose $100,000+ fines for each failure.

Lenders and the GSEs are tolerating bad appraisals and rewarding appraisers who can pump out reports despite their poor quality. Appraisers who are trying to provide good appraisals are disheartened by the sums of money being made by bad appraisers and tired of AMCs skimming off 40-60% of the appraisal fee. These issues are leading many good appraisers to give up and leave the business and still AMC's are attempting to hire the lowest bidder then complain about a "shortage" that they have created.

Solutions

- Federal Housing Finance Agency must push Fannie Mae and Freddie Mac to be less tolerant of bad appraisals and the lenders who use them. Failures should be quickly identified, and warning letters sent out in greater numbers.
- A larger number of SARs must be reported which will help law enforcement identify mortgage fraud and eliminate bad actors, fake borrowers, and poorly run institutions.
- Require lenders to directly pay for the services of AMCs rather than syphoning off a portion of the "appraisal fee" to pay for the appraiser's management.
- Establish separate lines on the loan disclosure form identifying the separate fees paid for appraisals vs. appraisal management.
- Prevent AMCs from shot-gunning appraisal orders out to dozens of appraisers at the same time in hopes of snagging the appraiser who will work for the lowest fee. When an AMC abuses this system there must be negative consequences for their actions.
- Force lenders and AMCs to seek out the best appraisers, not the cheapest.

We don't need new processes or systems as described in the RFI; what is needed is better enforcement of existing laws and guidelines. It will take some time, but the economic principle of supply and demand can and will solve the "appraiser shortage" as long as the Federal Housing Finance Agency pushes the GSEs to be better.

Richard Hagar, SRA
American Home Appraisals

What follows is an article, addressing the bifurcation of the appraisal process, that was published in a magazine sent out to more than 65,000 appraisers nationwide.

Why “Bifurcated” Won’t Work

By Richard Hagar, SRA

Bifurcated – divided into two branches or forks.
Bifurcated appraisal – appraisal process divided into two parts.

In other words, the appraiser sits in the office **never** viewing the subject or comparables; another person, usually a third-party that the signing appraiser has never met, visits the subject and comparables and “informs” the appraiser in the office about the quality, condition, view, and other value-influencing components of the subject and comparables.

Companies are selling the new lender-directed process as a way to “help” appraisers; a way to “free-up the appraiser so they can do more appraisals in a day by *avoiding* the time “wasted” driving to and from the subject.” They continue: “Appraisers should spend their time ‘appraising’ while someone else is trusted to inspect the subject.” Wow, it sounds like they are doing this for “our benefit”…with no expectation of any return for them.

We are hearing about the latest trend called *bifurcated appraisals*. Within the past year I’ve seen this term used more often in more diverse places than in the prior 20 years combined; it’s almost like some media company has decided that “bifurcated” is the “it” term for 2019/2020. All sorts of people, AMCs, lenders, technology companies, and Fannie Mae are promoting this “spiffy” new process. They are hoping that the rest of us will “get on board” with their new “better” process. I do not want to “get on board” because it’s headed for a train wreck.

Experiment

We have run several different experiments in our office: one where we have a trainee go out and inspect the subject property, and another where we’ve hired a real estate agent to do a walk-through “inspection” of a subject property (as a test, of course). The primary appraiser stays in the office while this other “person” inspects the neighborhood and the subject and reports back.

As an added measure, we even had the “inspector” drive by comparables that we pre-selected in advance. This is a step further than what Fannie Mae is currently proposing publicly. We’ve heard that Fannie Mae has been *testing* having inspectors drive-by comparables, and given Fannie’s vast database of photographs and property data, it is not inconceivable that Fannie could, in fact, share property photos of recently sold homes with appraisers who are attempting to select comparables without actually *seeing* them.

Be that as it may, what Fannie has been *saying publicly* about their proposed 1004P, is that the inspector will *not* drive by any comparables and the appraiser will have to go strictly off of what is on the MLS, or supplied by Fannie when selecting comparables to put into a report.

In our experiment, we had the appraiser pre-select what properties might be comparable and we sent the inspector out to inspect the exterior and interior of the subject, as well as drive-by the comparables.

Results
This process doesn't lead to better or faster appraisals or to a more accurate value conclusion, just the opposite. The latest property we tested this process with is a 1,600 sq. ft. rambler built in 1965 on a 10,000 sq. ft. site.

We sent our inspector out to inspect the subject and drive by ten properties that I selected which I thought might be good for comparison against the subject. The inspector supplied a sketch, photographs, and a description of the subject, as well as a description, and street side photographs of the comparables. This is when the process started to fall off the tracks.

Properties that, according to the photographs and inspection report, are ***inferior*** to the subject adjusted to an even lower value within the appraisal. This didn't make sense! They should have adjusted upward.

"Comparables" that appeared equal or slightly superior in quality and condition had their adjusted prices much higher than their recorded sales price. Higher? If they are "superior" their value should adjust down, not up. I used matched-pairs and/or regression analyses in determining adjustments for site size, quality, condition, and the house's square footage, but only a few of the adjustments helped narrow the value range. The adjusted value range was getting wider for some comparables and narrower for others—it didn't make sense.

Finally, after spending all day reworking the adjustments, cussing, pulling my hair out, and trying to make sense of this, I jumped in the car and drove by the subject and all of the comparables – I did the job that a competent appraiser normally does. *(What a concept!)*

What I Discovered
<u>Comparable #1:</u> Located only a few blocks from my subject, this is the same floor plan built by the same builder as mine (*Yea baby! Sometimes we get lucky*). While it had one additional covered parking space and looked to be in equal or maybe slightly superior condition, as compared against the subject that I hadn't seen, it was adjusting even higher. Why? Once I drove by, things became clear. This house was surrounded on three sides and across the street from newer, larger ultra-upscale homes owned by the super-rich. I didn't know that by looking at the MLS photographs and inspection report. While I was giving this "comparable" massive weight in my appraisal, I shouldn't have. This house ***wasn't*** being purchased as a place for a family to live in. Its primary value was the land, i.e. a lot suitable for construction of a new home for a newly minted Amazon millionaire. Even though it looked very, *very* similar to my subject, the house had no value, zip, nada, nothing. Well no wonder the adjustments for the extra garage space and condition didn't make sense, they were irrelevant! And even though the site was only a few blocks away, it's in an area far more desirable than my subject which required a location adjustment.

<u>Comparable #2:</u> The MLS reported a view but didn't included view photos. To me, that's an indicator that the view is very limited (or only from the bathroom window). There were photographs of the interior and they appeared to indicate that the home was remodeled and superior to the subject. Is this reality? Upon entering the driveway and getting close to the house… well what do you know, this house has a nice view looking out at the lake not the limited view reported by the MLS. In this area, that view contributed hundreds of thousands to the value. I didn't know that from the MLS photographs OR the inspector's photographs and notes. At this point, and I've only viewed comparables 1 and 2; I'm cussing out the inspector who didn't take time to drive all the way up the driveway and "discover" the view. And while the house appeared superior in the photographs, by the time I drove by, the contractors had

been there for weeks ripping out the interior. Oh, now I get it! It's a fixer! None of these items were properly reported by the inspector and only upon my more "hands-on" inspection was I able to perform a better comparison. For this one sale, I was missing more than $400,000 in adjustments!

Comparable #3: This third comparable was located up a gravel driveway and behind a home in terrible condition; previously I didn't know that fact. And while driving the neighborhood I discovered two new homes under construction. I took note, researched, and used their recent sales for establishing land value *(Sweeeeet!).*

The subject is in a plat with no restrictions…build whatever you want—big or small, nice, or basic. However, less than 200' to the South, the same street crosses into a subdivision with extensive restrictions; it has a requirement for the homes to be more than 3,000 sq. ft. and the design must be approved by the architectural control committee. Even though the subject is on the same street as the nice homes, it's located on the "wrong side of the tracks" where values are much less. This is additional valuable information that would have been unknown unless I *personally* visited the neighborhood. Once I drove by the subject and comparables, I discovered I wasn't adjusting correctly for the components that had major impact on value. The next day, back at the office, I began the whole description and adjustment process all over again and this time things started to come together—the right way.

What I describe above is not isolated; they are examples that I have experienced in most, not all, but most, of the bifurcated appraisals that we have performed in this office over the past few years. While some lender's "spiffy" new system might work in newer subdivisions of Phoenix or San Diego, where you have numerous similar home styles, it does not work in most of America where there are widely varying neighborhoods and houses.

During my inspection I learned so much more than I got with the MLS or inspector's photographs.

Overall

- If you haven't visited the neighborhood how do you know what remodeling or new construction is taking place, if any? New construction can be researched and used to establish land value for the subject, but you won't spot new construction unless you drive the neighborhood.

- Are neighboring properties being properly maintained or is a loud local motorcycle gang living next door and causing neighbors to flee?

- Is the neighborhood being updated or driven to abandonment? For instance, the City of Baltimore has 17,000 abandoned homes and is planning on tearing down more than 2,000 of these by the summer of 2020. Are some of the abandoned homes next to the subject? How about down the street, or next to the comparables? FHA and VA strongly suggest (if not require) photographs of anything that might impact the value of the subject…like an abandoned factory in a residential neighborhood of Cleveland. Will Fannie Mae's neighborhood report, that's spoon fed to us…or the inspector we are forced to "trust," inform the appraiser of the issue? No!

- Part of the appraisal process is reporting on conditions within the market area and neighborhood. Appraisers won't have an up-to-date-clue unless **they inspect** the neighborhood.

- How do you value or compare different view amenities –based on what someone else "sees" or "feels" about the subject or comparable's view?

- How do you verbally, or via a lender's checklist, convey a view amenity? Is there a 180-degree lake view or is it filtered through trees or limited by a roof across the street—for the subject, or the comparables?

- Was the inspector looking north or south when they took a photograph? And don't expect more than "a" photograph from them, it wastes their time. Was the view from the deck, bedroom, living room, or bathroom?

- Is that a high bank bluff waterfront or gentle slope? Don't you dare trust Google Earth 3-D to get it right. How does that compare with the comparables?

- Does the subject's granite countertop smoothly blend the slabs together or are there big ridges showing inferior workmanship?

- Is the sheetrock triple coated smooth Venetian Plaster or are they thick stucco covering the flaws?

- Do you feel a gentle slope to the floors indicating possible foundation problems or maybe a big bump under the carpet suggesting that the seller is hiding something?

- While inspecting a home, does the seller or the agent "let you in on a little secret about…….?" Don't expect the third-party inspector to stand still long enough to listen, they don't care; they are paid $50 per inspection.

- Are you really going to trust what some fast-moving property inspector says about the neighborhood and subject?

This system absolutely will not work for unique properties with view, acreage, waterfront, outbuildings, unusual style homes, or in neighborhoods where widespread remodeling is taking place; and how will you know if they are unique until the **appraiser** views them?

Part of the appraisal process is ***comparing*** the subject to the potential comparables. How do you properly "compare" when you have no basis, or starting point, for a comparison? Is this one better or is that one inferior? Why, and by how much, and for what reasons? Appraisers need to know because we have to "prove" our adjustments; we can't pull them out of the air based "on my 30 years in the business" attitude.

Allow me to be very blunt: anyone who promotes or suggests this is a "better way" to provide **residential** appraisals: A) has never properly appraised a residential property, B) doesn't know what they are talking about and/or, C) has a financial incentive to rip apart the appraisal process.

Let's take a high altitude look at the players pushing this "spiffy" new system: Fannie Mae is promoting it, big sloppy banks love it, an appraisal software company promises that it is "new technology" that will

somehow “help” appraisers, and a few AMCs think it’s a way to produce appraisals faster and pay appraisers even less. Does all of this really sound like a valid appraisal process?

The pressure has begun…all they need to do is convince a few suckers…er…appraisers that this bifurcated system complies will all state laws (it doesn’t), all federal laws (it doesn’t), and USPAP (maybe). So, to convince appraisers to “get on board” they use the *bifurcated* term often, touting it as the “newest thing” at appraisal trade shows. Remember it is your Certification that’s on the line here. Don’t trust them to tell you what is legal—they are just telling you their fantasy of how *they* want it to be – cheaper and faster.

Fannie Mae, Freddie Mac and some software company think technology is a solution. If their spiffy computers and algorithms failed to predict the crash of 2008, I bet they won’t predict the next one, until a year after it happens. Can you hear that? Do you feel the rumble? It’s a train going 80 mph toward a 25-mph curve.

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