Response of Better.com

to FHFA Request for Information

on Appraisal-Related Policies, Practices and Processes

February 2021

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**A1.1** Is there a need to provide new valuation solutions that address industry-identified issues of appraiser capacity, turn times, training, and rural and high-volume market coverage? What are those potential solutions? What are the risks of these policies and the challenges in implementing them?

New Valuations Solutions are Needed

Yes, because the industry-identified problems produce negative effects on the industry, such as increased cost due to lack of appraiser capacity, delayed turn times that extend the process (to the frustration of all stakeholders), and diminished access to credit. These effects can be acute in areas where the appraiser population is low, such as many rural areas. These trends preceded the COVID-19 pandemic. The pandemic has demonstrated the viability of solutions such as bifurcated appraisals. These solutions rely on available resources of non-appraiser professionals and technology to reduce the demand on a shrinking appraiser capacity.

Risk is to Accuracy

The risk presented by these solutions is to accuracy. The industry needs to test, and provide controls for, such solutions to ensure that stakeholders maintain confidence in these solutions. Data regarding cost, turn times, and CU scores will indicate whether such solutions satisfy market demands. In any of the reforms considered by the Enterprises, all parties engaged in data collection should have a minimum certification and apply pertinent standards, such as the ANSI Standards of Measurement. Without controls on the quality of the data collected, the data will have little value. Happily, most of the major challenges to implementing such solutions have been overcome as the pandemic has necessitated the adoption of these solutions.

Risk Present With Traditional Models, Necessitating New Tools

We note that without new valuation solutions, the concerns regarding accuracy would still be present. Prior to the pandemic, the demand for appraisers has reduced the time available for any individual appraisal, with commensurate impact on accuracy. Moreover, inherent and inevitable biases exist in appraiser-driven appraisals, which data from technology-driven solutions may reduce. Should the industry discourage solutions such as hybrid appraisals, the

accuracy risk will remain with no ready solution. The better approach is to add new tools to the appraiser’s toolbox, and work to ensure the accuracy of those tools through input from stakeholders, transparency, and testing.

**A1.2** Are there opportunities for process improvements that allow non-traditional valuation services (inspection-only, desktop, exterior-only) to augment traditional appraisals? Please elaborate on the risks, challenges, and benefits. Separately, are there opportunities to improve traditional appraisals to mitigate problems and concerns that have been observed to date?

**C1.1** What do you envision the impact of appraisal process improvements as described in this RFI to be on the appraisal industry? What impact, if any, has increasing use by the Enterprises of alternative appraisal solutions had on the availability and/or quality of traditional appraisals?

*Below response addresses both above questions.*

Let the Perceived Risk Determine the Valuation Method

Yes, ample opportunity exists for non-traditional valuation services to augment traditional appraisals. Because subject properties provide a broad range of facts and circumstances, the Enterprises should encourage the continued availability of a range of valuation methods. This will enable the use of the method best fitting to the facts and circumstances presented.

The valuation service applied should correspond to the risk presented by the subject property on the risk spectrum. Traditional appraisals will continue to be necessary for properties with high uncertainty or high risk. Hybrid, desktop, and exterior-only appraisals would address the

next three descending levels of risk. Property inspection waivers will be reserved for the lowest-risk scenarios, where the property was recently appraised and there has been no change of circumstances. This fact-driven selection would serve efficiency by conserving appraiser-capacity for where an appraiser is needed. Removing appraisers from unnecessary field work substantially increases capacity, especially as increasing use of automated tools facilitate report generation.

This approach would also reduce turn times because a significant percentage of valuations would not be traditional appraisals. This could also increase accuracy because a well-enunciated selection approach would increase process consistency across the industry, and enable more valid comparisons and scoring.

Likewise, the market presents opportunities to improve traditional appraisals, especially in the purchase context. The primary opportunity is to not anchor the appraisal to the sale price. Doing so should more fairly apportion the risk between the lender, the Enterprises, and the seller.

**A1.4** Would utilizing alternative inspection workforces, such as insurance adjusters, real estate agents, and appraisal trainees assist with addressing appraiser capacity concerns? Are there risks of using third-party non-appraisers? If yes, how?

**B2.5** What are the challenges associated with quality of service, enforcement and consumer protections related to non-appraiser entities providing property inspection data?

*Below response addresses both above questions.*

Proficiency and Conflict-Free Status are Essential Attributes of Any Alternative Workforce

While alternative inspection workforces can assist with addressing appraiser capacity concerns, the workforce should be selected with care to preserve the quality and reliability of the valuation. For the industry to provide a lender with the necessary security, the valuation process must utilize individuals that possess the necessary proficiency and are free of any conflict of interest. These issues will have ramifications both for the individual transaction and the industry. If inaccurate information is reported for an individual property, then the valuation will be inaccurate. Should lenders find an increasing number of inaccurate appraisals, their faith in the value of the industry’s services will be reduced. The diminishment of valuation as a reliable metric will increase the collateral risk borne by all, Below we address each individual alternative workforce:

● Real Estate Agents – Because a real estate agent’s compensation depends on the sale proceeding, and the agent has no financial risk thereafter, they are not a conflict-free workforce. This constitutes a disqualifying concern for their participation in the appraisal process.

● Insurance adjusters – Insurance adjusters do not suffer from a conflict of interest, but they lack the specialized knowledge and training to conduct significant appraisal services. With proper controls, they may be able to conduct certain activities that contribute to the appraisal (e.g., measure square footage) or taking photographs. However, their training will have to be rigorous and reinforced. The insurance adjusters will not experience the effects of poor execution in the same way the appraiser who is relying on the accuracy of the data will experience it. Moreover, the lack of information regarding any individual insurance adjuster is a control risk. Without that information, adjusters would avoid accountability and lenders would lack recourse. Not only is there no licensure requirement for adjusters, but the appraisal industry does not even capture the name of the adjuster. This lack of information creates undue risk for the lender.

● Appraisal trainees – Appraisal trainees are free of conflicts of interest, have appraisals as their primary focus, and possess substantial proficiency from their formal training. While they lack the experience of a certified appraiser, trainees can, with proper controls such as regular vetting of their work product, make a substantial contribution to the appraiser capacity concerns.

**A1.6** Do the objectives as outlined for the UAD update and form redesign meet the current and future needs of the mortgage industry. Are there opportunities for refinements or additions?

Standardization Promises Multiple Benefits, But Implementation Should Be Piloted and Phased to Ensure Reaping those Benefits without Undue Cost or Disruption

The standardization provided by the redesign will produce several efficiency benefits for the industry, including:

● Cost reduction – appraisers will only need to maintain a single form;

● Accuracy – with a new design that promotes consistency in reporting, accuracy

should be enhanced and the amount of revision to clarify or correct information

reduced;

● Turn times – a single form will reduce confusion and reduce the re-entering of information if the initial form type was inappropriate for the subject property;

● Appraisal reviews – Lenders would have access to CU scores for all form types; and

● Capacity – a single form would likely increase retention by reducing complexity, and facilitate new entrants to the industry (i.e., trainees) for the same reason.

However, such a fundamental change warrants risk management through pilots and phased implementation.

Questions on Risk Management

**B2.2** How can the Enterprises improve their collateral tools currently available to lenders? Include All Available Information in the CU Database

The Enterprises can improve the collateral tools by including information in the CU tool such as property type, whether the property has accessory dwellings (with detailed characteristics), and value estimates. If these tools show as much information regarding the property as possible, they will make a greater contribution to the lenders’ decision-making process.

**B2.6** Is there any data or evidence you could share regarding the performance of alternative appraisal solutions versus traditional appraisals?

Data Shows Strong Performance of Alternative Appraisal Solutions

Yes. The pandemic presented a crisis of opportunity to test alternative appraisal solutions, over an extended period and in a live market setting. Review of Better’s data from April 2020 through February 2021 demonstrates that alternative appraisal solutions performed either equal to or better than traditional appraisals. In the purchase context during the pandemic, desktop appraisals were cheaper (by $333 on average, or 39.1%) and with faster turn times (by 3.6%) than traditional appraisals. In the refinance context, exterior-only appraisals were cheaper (by $92 on average, or 16%) and with faster turn times (by 14%). In the aggregate, in the refi context, the alternative valuations produced moderate cost savings for the consumer, with little discernible difference in speed or CU score.

Time will tell if these loans performed at the same rate as loans with traditional appraisals. However, the gains of alternative appraisals solutions should not be understated. To undermine the demonstrated success of these tools the industry would need to see: (1) an increase in the default rate; (2) that increase is significant enough to exceed the risk appetite of key stakeholders; (3) that risk is attributable to the use of an alternative appraisal solutions; and (4) a traditional appraisal would mitigate that risk. With a broader perspective, the pandemic shows the need for a versatile toolbox for appraisers based on market conditions. Without alternative appraisals, the industry would have failed to satisfy demand. Without the Enterprises COVID flexibilities, the industry would not have fulfilled its role in real estate transactions, and not now know of the viability, and by certain metrics, superiority, of the alternative solutions.

Operational Questions on Appraisal Process Improvement

**C1.2** What would be the impact of appraisal policy and process improvements to the mid or late career appraiser? Do you believe late career appraisers would delay retirement if they could focus on specific valuation services like desktop appraisals? Or alternatively, would late career appraisers cease operations due to technology adoption challenges?

Alternative Valuation Solutions Extend Careers

Our experience over the last 10.5 months using a higher percentage of alternative valuation services indicates that such services have extended the careers of late-career appraisers and thereby increased capacity. Individual appraisers have explicitly informed us of this. While some late-career appraisers prefer traditional appraisals, in the aggregate, services such as desktop appraisals have increased career longevity. We also believe the UAD, by simplifying the process, would also extend careers.

**C1.3** Do you believe appraisal policy and process improvements would have a positive impact on access to credit, including for rural and underserved markets by providing additional valuation services that serve the needs of these markets?

Process Improvements Will Have a Positive Impact on Rural and Underserved Communities

Rural and underserved markets have the greatest need for policy improvements. These areas often lack suitable comparable sales, which increases the risk of a loan not being funded. These areas also have higher withdrawal rates due to longer turn times and lock extension fees due to those turn times. While we believe that these improvements would have a positive impact on rural and underserved areas, these improvements do not address the comparable sales and withdrawal issues identified above. To address those issues, the Enterprises should evaluate testing relaxation of time and distance requirements in several test locales.

**C1.4** Is there discrimination in current collateral valuation practices? If you believe there is discrimination, describe the impact. Please provide any relevant data or analyses to support your position. Conversely, are there concerns that alternative or automated solutions could have a discriminatory impact?

Restore Appraisal Integrity By Restoring Appraisal Design’s Three-Legged Stool

Yes, current valuation practices discriminate against minority borrowers both through individual bias (whether conscious or unconscious) and structural bias. We believe a candid acknowledgment of discrimination by the industry is the sine qua non of fair treatment of all borrowers, and measuring risk with integrity for all stakeholders, including lenders. The most significant structural bias is overreliance on the sales comparison approach to value.

We note that the vast majority of U.S. neighborhoods remain segregated by race because of official governmental policy. Rothstein, Richard. *The Color of Law: A Forgotten History of How Our Government Segregated America*. New York City, Liveright, May 2017. Measuring an individual property’s value by the [racial composition](https://www.bloomberg.com/news/articles/2020-09-21/race-gap-in-home-appraisals-has-doubled-since-1980?sref=lfUVr41V) of the neighborhood is a legacy of the now-illegal practice of redlining. Research shows that homes in non-minority neighborhoods are appraised at higher values than homes in minority neighborhoods, even when property and neighborhood characteristics are held constant. Hipp, J. and Singh, A. (2014). “Changing Neighborhood Determinants of Housing Price Trends in Southern California, 1960-2009.” *City and Community* 13(3):254-74. [Changing Neighborhood Determinants of Housing Price](https://journals.sagepub.com/doi/full/10.1111/cico.12071)  The delta is not trivial. In fact it is enormous. After controlling for house characteristics including square footage, fireplace, garage, patio, and pool, and neighborhood characteristics such as average house size, vacancy rate, poverty, crime rate and parking, the homes in minority neighborhoods are appraised at 41.4% of homes in non-minority neighborhoods. “The Increasing Effect of Neighborhood Racial Composition on Housing Values, 1980-2015.” *Social Problems*, 0:1-21. [Increasing Effect of Neighborhood Racial Composition on Housing Values](https://academic.oup.com/socpro/advance-article-abstract/doi/10.1093/socpro/spaa033/5900507?redirectedFrom=fulltext) Because this racial analysis fosters the view that minority neighborhoods are less desirable, the heavy weighting of the sales comparison approach perpetuates the undervaluing of minority neighborhoods. Howell and Korver-Glenn (2020).

When a practice accepts racial composition as an input, the practice ceases to measure the value of a property, and instead measures race. The obvious impact of this is the deleterious effect on minority homeownership and wealth creation. Undervalued properties skew mortgage ratios making borrowers in minority neighborhoods less likely to qualify for a mortgage. Undervalued properties reduce the proceeds minority homeowners receive upon sale.

But economic metrics tell only half the story. The other half are the self-cancelling adaptations minority homeowners implement to mitigate the economic damage. Minority families are familiar with the depressing chore of [erasing](https://www.nytimes.com/2020/08/25/realestate/blacks-minorities-appraisals-discrimination.html) evidence of themselves (family photos, African-American, HBCU degrees) from their homes, and absenting themselves physically from the appraisal process, to reduce the risk of their home being identified as Black-owned. While

multiple tools are necessary to eliminate discrimination in valuation, here we identify two early steps: (1) restoring the stability offered by the three-legged stool of the sales comparison approach, the income approach, and the cost approach; and (2) balancing human analysis with technological analysis of the property.