BUSINESS

Will New Appraisal Rules Help Or Harm?

By KATHLEEN DOLER, FOR INVESTOR'S BUSINESS DAILY
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A Realtor's sign goes up outside a house in Chagrin Falls, Ohio. The process for appraising home value is changing, in ways that could affect sales. AP

New appraisal rules meant to ensure fairness are being blamed for ugly side effects.

Getting a fair appraisal is actually harder now, some real estate agents say, especially on a top-flight property. They warn that could depress prices, spur buyer-seller disputes and raise problems with refinancing.

The rules kicked in over the past two months. Appraisers worry that strict interpretation by colleagues and lenders is leading to artificially low home valuations.

"The new appraisal rules are artificially repressing the market and artificially repressing the (housing market) recovery," said Gary Crabtree, an appraiser in Bakersfield, Calif.

On April 1, Fannie Mae (FNM), Freddie Mac (FRE), the Federal Housing Administration and the Veterans Administration began requiring that a new appraisal form be filled out for each new loan to be backed by these entities. This "market conditions" addendum requires analysis of median prices for comparable properties, over a variety of time periods. It also requires data on housing inventory and absorption. Fannie calls it Form 1004MC, and Freddie Form 71.

Who Can Order Reports

On May 1, Fannie and Freddie implemented the Home Valuation Code of Conduct. It makes lenders submitting loans for backing by the two ensure that appraisals are managed independently of loan originations.

If a lender has its own appraisal management company, it must operate independently of the loan unit. Loan brokers bringing mortgages to Fannie and Freddie for backing can no longer order appraisals — they must use an appraisal management company that assigns appraisers.

This independence rule arose after New York Attorney General Andrew Cuomo began probing the appraisal business and filed suit against First American Corp. (FAF) and its eAppraiseIT unit. The suit alleges the unit let loan staff at its client Washington Mutual pressure appraisers to inflate home values.

Cuomo subpoenaed Fannie and Freddie, but dropped his review of their appraisal practices after they agreed to set new appraisal rules for loans they back. Thus the Home Valuation Code of Conduct was born.

But appraisers say it is deeply flawed. They ask how independent appraisal management companies can be, since lenders own many. And having these outfits assign and manage appraisals means they determine appraisers' fees and deadlines.

Bill Garber, director of government and external relations at the Appraisal Institute, has heard from numerous appraisers that some appraisal management firms are slashing appraiser fees. And they may ask appraisers to do reports in 24 hours or less, threatening quality — the industry standard is three to five days.

"Now is not the time for a flight away from quality and experience," Garber said.

Some veteran appraisers won't work for the management firms.

More For Less?

Appraisal prices range from about $300 to $500, depending on the region and home size. But Crabtree says appraisal management firms are trying to pay as little as $200 and hire "geographically incompetent" appraisers cheaply from outside an area. He's seen appraisers come into Southern California from as far away as Nevada, with no knowledge of local markets or neighborhoods.

"It's the only job in the world where the better you are at doing it, the more experience you have, the less you get paid," said appraiser George Dodd, in Mechanicsville, Va.

Homebuyers have little control of appraisals, despite paying for them.

Appraisers say competent appraisers were already analyzing median prices before the market conditions form became required. But they worry that inexperienced appraisers will rely too much on median prices for their reports, and lenders may reject appraisals that value properties above median prices.

Appraisal problems spill down to buyers and sellers in several ways.

Price Problems Arise

Southern California home rehabber Chris Kostecka says since the new form arrived, he's had trouble getting homes he's refurbished to appraise for his selling price, even when he's received multiple offers.

If homes are appraised off of median prices today, when foreclosures are a majority of sales, that will put more downward pressure on prices, says Guy Cecala, publisher of Inside Mortgage Finance, in Bethesda, Md.

If homeowners can't get decent appraisals, to sell or refinance, it may push more into default, Cecala says.

Another risk is if a home doesn't appraise for the offer price, a buyer may walk away. Or the lender may require a larger down payment. But the seller may reduce the price or finance some of the difference to enable the sale to go through.

Buyers or sellers can get an independent appraisal for their own review, beyond what a lender orders.

More change could be ahead, as Congress is weighing in. The House of Representatives passed mortgage reform bill H.R. 1728 in May, and the topic has now moved to the Senate. Aimed at curbing predatory lending, the House bill includes measures for studying and ensuring appraisal quality, and setting new oversight of appraisal management companies.