

Good morning. My name is Steven Berg. I am a real estate appraiser and consultant, practicing in Portsmouth since 1987. In 2003 I was appointed to the NH Real Estate Appraiser Board and I now serve as its Chair. We are the board responsible for licensing appraisers to work for you. There have been some major changes regarding the regulation of appraisers in only the past few months and there are probably more to come. I am here today to share with you those changes and my outlook, as well as to discuss how this impacts lenders.

Before I go on, I should give you a little background. Many of you have probably heard of FIRREA, the Financial Institutions Reform, Recovery and Enforcement Act. This was a sweeping bank reform act passed by Congress in 1989. Amongst its provisions was the requirement that appraisals for banks be performed by state certified appraisers. The Appraisal Foundation is a non profit educational entity, established within the appraisal profession to promote uniform standards of practice. With FIRREA, Congress essentially made the Foundation's mission an official responsibility. The Foundation has two divisions: The Appraiser Qualifications Board or AQB, who establishes the requirements for becoming an appraiser, and the Appraisal Standards Boards, or ASB, who writes and updates the Uniform Standards of Professional Appraisal Practice, or USPAP. In the packages I have handed out are some brochures from the Foundation, the AQB and the ASB.

It is the responsibility of the State Appraiser Boards to implement and enforce the requirements that come down from the AQB and the ASB. We are free to add requirements, or implement stricter requirements, but the Foundation mandates the minimum requirements. Until only recently, it had been relatively easy to obtain a license. The advent of appraiser licensing lulled lenders into believing that their appraisers need only be licensed by the state; this is simply not true. The simple possession of a license does not imply competence, knowledge, or ethics; it only means that its holder has met a minimum set of criteria. At the time, a great many appraisers exceeded these criteria and this is still true today. The Merriam Webster dictionary defines profession as "a calling requiring specialized knowledge and often long and intensive academic preparation". While many appraisers meet this definition, many do not. As the sub-prime crisis continues and more stories about mortgage fraud appear, it will grow increasingly clear to you just how many appraisers are not professionals.

The primary change in the appraisal world came on January 1st of this year. This was the deadline for all states to enact the AQB's significantly more difficult requirements for obtaining credentials. There are three basic requirements to become certified as an appraiser: Education, Examination and Experience. The changes relate primarily to education. All levels of credential now require substantially more classroom hours. Also, each level of credential now has a specific curriculum requiring a certain number of hours be spent on each of a number of specific topics. A candidate for general, or commercial certification, the highest level of credential, previously had to complete 180 hours of education. All but 50 of those hours could be carried over from their residential education and none of the courses had to cover much in the way of specific topics. Now, 300 hours is required and most of it must be spent on topics specific to non-residential appraisal. In your handouts is information itemizing these changes.

The toughened educational requirements now culminate with a new national uniform exam. As of January 1st, the required examinations became much harder. These exams now actually test a candidate's ability to recall information learned in qualifying education offerings as well as their ability to apply that knowledge in solving real appraisal problems. These exams can not be passed by cramming definitions and formulas the night before the test. The tests are also much longer. For example, the general certification test went from having four hours to complete 125 questions to eight hours and 165 questions.

The one last educational change is that certified residential appraisers must have an associate's degree and certified general appraisers must have a bachelor's degree. Going forward, you, as users of these appraisal services can expect that new appraisers will, as a rule, have a significantly stronger educational background. Hopefully, this will increase the quality of the work your banks see. Unfortunately, these changes are not retroactive.

I should mention also that the slowdown in the housing market is reducing the ranks of appraisers. In NH, excluding trainees, 527 license renewal applications were due by December 31st; 104 were not returned. In Maine, 45 out of 300 applications were not returned. Both states stagger their renewals annually, so we can probably expect more to drop out at the end of this year. At the risk of generalizing, I think that it is safe to say that most of the people giving up their licenses are people who saw this as their job, not their career. The departure by at least some of these people may be a good thing. Recall also that if these folks try to reenter the profession, it will be at the new criteria.

Another big problem that both the New Hampshire and Maine Boards have seen, are abuses by supervising appraisers. Many unethical appraisers have taken under their wings a great many trainees. First, there are only so many trainees any person can train and supervise. But what is happening all too frequently is that these under-trained trainees are being sent all over creation, by themselves, to do appraisals. The supervisor then signs the reports saying that he or she also inspected the subject, when they did not. Some are even accepting sole responsibility, not even mentioning who actually did all the work. From my perspective, this is unethical and illegal in too many ways to cite here. From your perspective, you may be getting appraisals from people who are not qualified to do them, and you don't even know it. The new 2008 changes attempt to put a stop to this by mandating that supervisors can have no more than three trainees at a time and that supervisors must be certified, as opposed to only being licensed. In NH, we have toughened this new rule to stipulate that supervising appraisers must also be a New Hampshire certified appraiser, and must have been a certified appraiser for two years.

This brings up another problem: too many lenders will not hesitate to use appraisers from out of town because they are faster or cheaper. I probably do not need to say this to those of you who are here today, but fast and/or cheap appraisals are not in the best interest of your institution. In fact, quite often, the reason they are fast or cheap is that you are getting the under qualified trainee ... at best! At worst, you are getting somebody so desperate for work, they will do whatever it takes to ensure continued work from you.

Until all of these toughened requirements truly take hold, this industry will be in transition. A large part of the burden to accelerate change lies in the hands of the users of

appraisal services. We all know that the overwhelming majority of those users are you: lenders. When you see a bad or unethical appraisal, do something about it. The Appraiser Board's in each state have the responsibility to police poor conduct, but we are not a police department. We simply do not have the resources to go patrolling looking for violators. Therefore, we rely on complaints. In 2007 only 21 complaints were received by the NH Board and 37 were received by the Maine Board. In both states, only a few complaints were lodged by lenders.

As regulators, what are we supposed to do if the largest users of appraisal services are the most silent? Unfortunately, you may soon be required to report problems. A major banking reform bill now before the US House of Representatives contains a provision requiring lenders to report fraudulent appraisals. Your handouts contain a link to the text of HR 3837.

I am asking you to help me improve my profession, but it is your best interest! You need only look at the current mortgage crisis. Generally speaking, sound underwriting of loans is based on the "Three C's" – credit, capacity to repay, and collateral. If there are weaknesses in any of these areas, the loan carries greater risk. The boom in sub prime lending represented a boom in loans that had higher risk relating to the first two C's: credit and capacity to repay. This makes the valuation of the collateral -- the appraisal – even more important. Real estate appraisals play an important role in protecting both financial institutions and borrowers. But instead of the lending industry as a whole embracing the importance of the appraiser's role, many lenders, particularly mortgage companies with fewer regulations, saw appraisals as an obstacle in the path to more commissions. The result was an enormous increase in the pressure exerted on appraisers to "hit the number".

Appraisers must remain independent. We are ethically required to provide our opinion in an unbiased manner. You are going to be hearing the phrase "appraiser pressure" quite a bit in the coming years. Too many appraisers are being pressured into providing an appraised value that makes the deal work. In some instances, appraisers who refuse to bow to such pressure are placed on exclusionary lists or are simply not paid. Federal bank regulatory agencies report widespread breakdowns in appraisal independence. Unfortunately, institutions outside of the purview of federal bank regulatory agencies drive much of the mortgage market, and they are able to do so with very little regard to appraisal requirements. Far too many appraisers have given in to that pressure, were simply incompetent, or were blatantly unethical. The spotlight that is now shining on all of the foreclosures, particularly in the sub prime market, has also illuminated the collateral valuation problems.

In 1999, the Appraisal Standards Board issued an advisory to appraisers explaining what constitutes appraiser pressure and how we are ethically required to handle it. You should read Advisory Opinion 19; I have given you the link to it on the Appraisal Foundation's web site. It may shock you to learn that you have probably, unintentionally, committed appraiser pressure. I bet that many of you have a space on your appraisal requisition forms that says something like: "Estimated value: \$300,000". I completely understand that most of the people in this room mean that only as an FYI. It may even just be a request that the appraiser give you a "heads up" if there are any problems so you will know to wait before you order title work. But how do you know that the appraiser, or worse yet, a

regulator or other third party, won't see that statement as code for: "you need to appraise this house for \$300,000 or you will not get any more work from us"? You know you don't mean it that way -- and you are probably shuddering at the implication -- but there are lenders that do mean it that way, and they use the exact same statement: "Estimated value: \$300,000".

As ethical lenders, you need to understand that it very common for mortgage lenders, mortgage brokers and others to use only those appraisers who "hit the number" regardless of whether it represents market value. This is what happened with Washington Mutual, or WaMu. Yes, WaMu pressured First American into providing appraisals that met the mark, but maybe you do not know who First American is. Through their subsidiary, E-Appraise IT, First American is an appraisal management company, or AMC. AMCs primarily obtain appraisals on behalf of their clients; they do not actually perform the appraisals. WaMu instructed First American to provide them with appraisals performed by "proven appraisers". These are appraisers who regularly hit the mark. They might have done so out of incompetence, greed, or fear, but these are appraisers who provide an appraisal for \$300,000 when told, "Estimated value: \$300,000". These bogus appraisals, which number into the tens of thousands, were not the result of bribes or kick-backs. They were performed by appraisers acting only under the presumption that doing so would guarantee more assignments. This fraud represents the actions of thousands of appraisers willing to flush their lives down the drain for \$275!

To some degree, this is nothing new. But it is now much worse. Ninety percent of appraisers surveyed in 2006 reported being pressured to hit the number. This same survey only three years earlier, showed 55% of the appraisers reporting pressure. I will do what I can to stop other appraisers from committing fraud, but you as lenders need to stop other lenders from asking the appraisers to commit fraud.

Look at the nature of mortgage lending in the 21st century. Mortgages are no longer a useful service provided by our local lenders. Mortgages have become another product sold to consumers. WaMu refers on their web site to their network of 2,700 "consumer and small business banking stores". Not banks, not loan origination centers, but "stores". The people who work in these stores are sales people. We call them loan officers and originators, but make no mistake about it: these are commissioned sales people who will make thousands of dollars on each mortgage they sell. Like all salespeople, their sole motivation is to sell as many of these that they can. Bank officers are truly motivated and given an incentive to act in their bank's best interests, mortgage sales people are not. As a result, I actually burst out laughing when I read the denial that WaMu issued in response to the First American accusation. They said, in part:

We are surprised ... by the allegations in the complaint ... We have absolutely no incentive to have appraisers inflate home values. In fact, inflated appraisals are contrary to our interests.

It may not be in *your* best interest Washington Mutual, but what about the tens of thousands of sales people you have staffing your 2,700 mortgage stores? Did anybody tell them that? The day the accusations were levied, WaMu terminated its relationship with First American. Does anybody know if any originators were let go? I have no idea, but I doubt it.

The best sales people are those who get things done. It is not unreasonable to expect one of these salespeople to pick up the phone and ask an appraiser to take a second look at their conclusion. It may be a completely innocent request, but the request is being made by a skilled sales person, highly trained in the art of persuasion. On the other end of the phone is an appraiser who is extremely sensitive to these sorts of requests. In addition, the appraiser is afraid of losing a client. Therefore, any request to reconsider an appraised value, no matter how well intended, is in and of itself, unwelcome.

If you haven't already, I urge you to read the new policy that Fannie and Freddie propose to adopt January 1, 2009. The link is among your handouts. One provision calls for the establishment of an agency to receive and investigate allegations of appraiser pressure. If pressure is found to have occurred, Fannie and Freddie will end their relationship with that lender. There is pending legislation at the federal level, and in many states, including New Hampshire, that will outlaw appraiser pressure. Frankly, Fannie and Freddie's actions will likely have a more immediate and more far reaching impact because economic pressure is much more effective than government pressure. By the way, NH is expected to pass the appraiser pressure legislation this month; the text of the new law is in your packages.

There is an enormous public benefit to stopping the practice of pressuring appraisers. I am very concerned though that we are now witnessing the start of an enormous backlash by appraisers. All appraisers, most of whom are ethical, are fed up with the pressure tactics. Now, as a result of the efforts to stop it, appraisers are becoming empowered. That may not be good news for lenders. Soon, incompetent and unethical appraisers will be able to deflect at least some of the blame by screaming: "Appraiser pressure!! Appraiser pressure!! I didn't want to do it but they made me!" It sounds absurd, but we have a rich tradition in this country of blaming others for our own transgressions. False allegations will simply fan the flame. That runs a very real threat of taking resources away from where the problems actually lay. I do not envy you lenders right now. I do not how you are going to fend off the false accusations.

Banking trade groups are actively involved in the solution. That is important, but I also urge you to get involved on your end. My second concern, in addition to the bad appraisers crying wolf, is that this will become a battle of the lending community versus the appraisal community. There are major problems within both of our professions that have merged to bring out the worst in each. Blame is a waste of energy; we need to work together to restore professionalism to the entire system.

Finally, before I open up the floor to questions, I want to touch upon the mortgage fraud problem. Your keynote speaker at this conference is an expert in the outwardly criminal aspects of mortgage fraud. As a result, I have left that aspect of problem appraisals out of my comments today. As Mr. Siciliano discusses the problem with you, please remember that almost every scam he talks about requires the cooperation of a real estate appraiser. Ethics and morality aside, the only participant in nearly every type of mortgage scam whose job it is to actually prevent the scam from happening is the real estate appraiser. My term on the State Board ends in 152 days. I am quite fond of the person who will be my successor as Chair, so it pains me to tell you that you are all invited to the party where I will be celebrating the fact that all of this is now somebody else's problem.

Supplement to Presentation Made by Steven Berg at the 2008 Tri-State Mortgage Conference

The Appraisal Foundation

<http://www.appraisalfoundation.org/>

(For copies of the handouts, “ASB & USPAP” and “Executive Summary of 2008 Real Property Appraiser Qualification Criteria”)

NH Real Estate Appraiser Board

<http://www.nh.gov/nhreb/>

(for new education requirements and other useful links)

HR 3837 Escrow, Appraisal, and Mortgage Servicing Improvements Act

<http://www.govtrack.us/congress/bill.xpd?bill=h110-3837>

USPAP Advisory Opinion 19 – Regarding Appraiser Pressure

<http://commerce.appraisalfoundation.org/html/2006%20USPAP/ao19.htm>

Agreements between NY Attorney General and Fannie Mae & Freddie Mac

http://www.oag.state.ny.us/press/2008/mar/mar3a_08.html

Text of NH’s Proposed Appraiser Pressure law

Amend RSA 479 by inserting after section 30 the following new section:

479:31 Undue Influence Prohibited; Penalty.

I. No person with an interest in a real estate transaction involving an appraisal shall improperly influence or attempt to improperly influence, through coercion, extortion, bribery, or threat, the development, reporting, result, or review of a real estate appraisal sought in connection with a mortgage loan. This shall not prohibit a person with an interest in a real estate transaction from asking an appraiser to do any of the following:

- (a) Consider additional, appropriate property information.
- (b) Provide further detail, substantiation, or explanation for the appraiser’s value conclusion.
- (c) Correct errors in the appraisal report.

II. Any person who violates this section shall be guilty of a misdemeanor. If a person who violates this section is licensed under any state licensing law, a violation of this section shall be deemed a violation of that state licensing law.