Push to cut back on home appraisals sparks controversy

(Caspar Benson / Getty Images)

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The Nation’s Housing

NOVEMBER 26, 2018, 11:10 AM

The Trump administration wants to eliminate professional appraisals on a large number of home-sale transactions — a move that critics say could push the country back toward the see-no-evil days of mortgage lending that preceded the housing crash.

Just before Thanksgiving, the administration's top financial regulators — the Federal Deposit Insurance Corp., the Federal Reserve and the Treasury Department's Office of the Comptroller of the Currency — issued a joint proposal that would make traditional appraisals unnecessary for many new mortgages originated for less than $400,000. Instead of a formal appraisal, these homes would receive an “evaluation” by individuals who have no appraisal licenses or certification and would not be subject to current state regulatory oversight requirements that govern appraisers. The evaluators could be an “independent bank employee” or unnamed “third part(ies).”

They would, however, have to be “competent” and possess “knowledge of the market, location and type of real property being valued.”

The goal in loosening standards is to lower costs and reduce time in home-mortgage transactions, according to the agencies. There is already an exemption from mandatory appraisals for new mortgages less than $250,000 when a loan is not intended to be sold to government-backed investors such as Fannie Mae or Freddie Mac, insured by the Federal Housing Administration (FHA) or guaranteed by the Department of Veterans Affairs (VA).

The new proposal would increase the $250,000 ceiling to $400,000, significantly expanding the reach of the no-appraisal approach. The agencies estimate that if their plan had been in place during 2017, approximately 214,000 home transactions would have been affected. The median existing home price nationwide in October was $255,400, according to the National Association of Realtors, far below the proposed $400,000 threshold.

Appraisers are reacting to the regulators' plan with outrage — not surprising given the dent it could leave in their incomes. But appraisers say the issue goes far beyond money and instead gets to the “safety and soundness” responsibilities the federal agencies have concerning banks and mortgage lenders. Without a truly independent, professional valuation of a home — its interior, exterior and recent comparable sales — the door could be open to more loans on houses with inflated appraisals designed to "hit the number" needed by the lender to close the deal.

James L. Murrett, president of the Appraisal Institute, the country's largest group representing appraisers, says adoption of the plan would represent “a return to the loan production-driven environment seen during the leadup to the financial crisis, when appraisal and risk management were thrown aside to make more — not better — loans. Apparently, the nation's bank regulators have learned nothing from that experience.”

Ryan Lundquist, an appraiser in Sacramento, Calif., says the financial regulators’ claim that cost is a motivating factor in their proposal is bogus. “In reality,” he says, “the appraisal is one of the least expensive elements in a transaction, especially when compared to what loan officers and the banks make.” Yet at the same time, it is one of the most important for consumers. On a $350,000 home purchase, a $500 appraisal represents 0.0014 percent of the cost. For a home buyer, a professional opinion of value serves as a check on whether the house is priced too high.

Pat Turner, an appraiser active in the Richmond, Va. market, told me if the regulators' goal is to reduce time and costs, they should cut back on the role of “appraisal management companies,” middlemen who add anywhere from 40 percent to 50 percent or more to what the home buyer pays. Management companies are involved in the majority of new mortgage transactions; they choose the appraisers for assignments, review the valuation and send it to their lender clients. When the home buyer is charged $500, Turner says, the appraiser may only be receiving $250, while the management company pockets the other half. Without the middleman, the appraiser might charge $350, and that's all the buyer would pay — a $150 saving.

Equally relevant, he says, is that the presence of management companies in the transaction inevitably adds “days to the whole process.” Turner also notes that evaluations typically do not involve interior inspections, so the value estimate is missing a crucial set of observations. The house might have serious interior or structural damage that lowers its true market value. But if a bank only sees an "evaluation" with no interior inspection, it might well have no clue.

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