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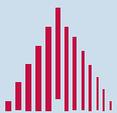
Roundtable



NEW WORLD OF **APPRAISALS**

What are the options?

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NEW WORLD OF APPRAISALS

WHAT ARE THE OPTIONS?

Toward the end of *ABA Banking Journal's* sponsored roundtable on appraisal trends, one of the bankers participating turned and asked the four appraiser panelists: "I just have to ask: Did you come here thinking it was going to be 'Us versus Them?'"

Actually, the appraisers had wondered the same thing. But after two hours of intensive discussion, both sides ended up not only knowing a lot more about their respective businesses and the role that appraisals play in real estate-related lending transactions, but had an enhanced respect for each other's expertise and professional commitment.

The four appraisers participating were all officers of the Chicago-based Appraisal Institute, the worldwide professional association that was sponsor of the event. Two of the bankers were commercial real estate lenders and two were from the residential side.

Ten years ago, such a gathering would have had a different focus. Back then, virtually all aspects of real estate finance—commercial and residential—were still in boom times when the actions of a few tarnished the reputations of all. These participants are all survivors of that era and of the major correction that followed. Now, however, they all must abide by the truckloads of new rules and regulations for appraisers and bankers alike. The eight participants are all experienced players. They are more than survivors—they are the cream of the crop. Thus, they were an ideal group to explore three main themes:

- **Appraiser independence**—foundational changes resulting from the 2009 Home Valuation Code of Conduct (HVCC), now incorporated into the Dodd-Frank Act;

- **Examination issues**—the ongoing effects of overzealous examiners calling for reappraisals of properties; and

- **Appraisal options and services**—when to use automated valuation models and broker price opinions versus full appraisals.

Following are brief descriptions of the participants and their institutions.

Richard L. (Rick) Borges II, MAI, SRA, is 2013 president of the Appraisal Institute, an organization with 23,000 members in 60 countries worldwide. Borges has 40 years experience in the real estate business. He runs a full-service appraisal firm in



There certainly are ways to establish independence of appraisers and firewalls without AMCs



Rick Borges

ALL INSIDE PHOTOS: ARNOLD ADLER

OUR ROUNDTABLE PANELISTS

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MAI, SRA**

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John P. Brodrick

SENIOR VICE PRESIDENT,
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**M. Lance Coyle,
MAI, SRA**

VICE PRESIDENT
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DALLAS, TEX.



Jay Forrester

GROUP VICE PRESIDENT AND
SENIOR LOAN OFFICER
GEORGIA BANK & TRUST CO.,
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Cynthia Lowman

PRESIDENT, UNITED BANK
MORTGAGE CORP.
UNITED BANK OF MICHIGAN,
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Elizabeth Magennis

EXECUTIVE VICE PRESIDENT AND
CHIEF LENDING OFFICER
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Sara W. Stephens, MAI

IMMEDIATE PAST PRESIDENT
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**Ken P. Wilson,
MAI, SRA**

PRESIDENT-ELECT
APPRAISAL INSTITUTE,
PLANO, TEX.



William Streeter

EDITOR AND PUBLISHER
ABA BANKING JOURNAL,
NEW YORK, N.Y.



Indiana with his wife, LaVonne, doing appraisals, property development and management, as well as mediation and arbitration of real estate value disputes around the country.

John P. Brodrick, senior vice-president, Eastern Bank, Boston, Mass. Brodrick oversees mortgage and consumer financing areas of the \$8 billion-assets mutual savings bank, and is responsible for business development and revenue for mortgage, indirect auto, credit cards, and home equity.

M. Lance Coyle, MAI, SRA, vice-president, Appraisal Institute. Based in Dallas, Tex., Coyle is an appraiser who has a small litigation support practice providing expert witness testimony in commercial property litigation cases.

Jay Forrester, group vice-president and senior loan officer, Georgia Bank & Trust Co., Augusta, Ga. The bank is part of a \$1.7 billion-assets, two-bank holding company that straddles the border with South Carolina.

Cynthia (Cindy) Lowman, president, Mortgage Corporation, United Bank of Michigan, Grand Rapids, Mich. The mortgage corporation is a wholly owned subsidiary of the \$448 million-assets family-owned bank.

Elizabeth (Liz) Magennis, executive vice-president and chief lending officer, ConnectOne Bank, Englewood Cliffs, N.J. The \$929 million-assets bank, formerly North Jersey Community Bank, focuses on commercial real estate lending.

Sara W. Stephens, MAI, immediate past president, Appraisal Institute, Little Rock, Ark. Stephens and her husband, Richard, have a diverse practice, including litigation support, easement work for acquisitions, and commercial property appraisals. They had a large residential practice for many years, but now focus on commercial work.

Ken P. Wilson, MAI, SRA, president-elect, Appraisal Institute, Plano, Tex. A 35-year veteran of the appraisal business, Wilson is a sole practitioner handling appraisals for all property types, but focusing on commercial. Currently, he is doing mainly review appraisals.

Panel moderator was *Bill Streeter, editor and publisher, ABA Banking Journal, New York, N.Y.*

Here is the edited session report.

APPRAISER INDEPENDENCE
The 2009 HVCC was largely incorporated into the Dodd-Frank Act and continues to ripple through the home-

mortgage market. What was the problem it was intending to address? Is it doing that—or is it overkill?

Rick Borges What it tried to address was the possible coercion that appraisers felt to conclude higher values to facilitate the issuance of loans. It seems there is now some coercion that appraisers feel *not* to generate a value that enhances the transaction or causes it to occur, because they're scared of enforcement agencies. The Appraisal Institute's view would be to hire the best appraisers—and we think they're our Designated members—allow them to do their job, and view them as trusted professionals.

Lance Coyle The idea was to set up a firewall between the person ordering the appraisal, who, in theory, has something to gain, and the appraiser, who is supposed to be completely independent. In practice, unfortunately, the code has created a lot of problems that were not anticipated, and it's probably the biggest complaint on the part of appraisers. It is particularly acute on the single-family mortgage lending side where, in many cases, the lender response has been to hire an appraisal management company (AMC) that fulfills the role of the firewall. The common complaint we're hearing is that the AMC is taking half the fee. A residential appraiser might charge \$350 for a standard-form appraisal, and the management companies take half. The other complaint we hear from Realtors and bankers is that the AMCs don't particularly care who is best for the job. So, you might get somebody hired and sent 50 miles away to do work where they may not be geographically competent.

Liz Magennis We had a property in northern New Jersey, and there was an appraiser assigned from Lakewood, which is an hour and a half south of us—a completely different market—who was coming to appraise the prop-



When the Dodd-Frank appraisal rules came out, we had to explain this new fee to our customers

Jay Forrester



Not all properties are the same.

Neither are all appraisers.

Minimizing loan risk is a top priority for every lender; after all, it's your bank's bottom line that's ultimately on the line. Whether you hold commercial or residential loans, you need objective appraisals to help guard against inflated valuations or mortgage fraud. That's where Appraisal Institute professionals with the **MAI**, **SRPA** or **SRA** designations come in.

From specialized knowledge and experience valuing different classes of property to foreclosure appraisals and advising on complex regulatory compliance issues, Designated members of the Appraisal Institute have the experience, integrity and knowledge to help lending professionals better understand complex real estate valuation issues.

By working with unbiased, experienced and professional appraisers of the Appraisal Institute who are committed to conducting business in accordance with the highest ethical standards, you can tap into the specialized expertise of the nation's premiere real estate appraisers. In addition to meeting state licensing and certification requirements, all Appraisal Institute Designated members must also adhere to the Appraisal Institute's strictly enforced Code of Professional Ethics and Standards of Professional Appraisal Practice.

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erty. It just didn't make sense to hire a firm that is not closely familiar with a particular market.

Coyle One of the unintended consequences of this has been that we've destroyed the business relationship between bankers and appraisers.

Sara Stephens That's gone away in the name of very quick turnaround time and very cheap fees. And having someone come in from 100 miles away with the lowest fee and a fast turnaround time doesn't necessarily net the expertise you need.

Is using an AMC a requirement?

Borges There certainly are ways to establish independence of appraisers and firewalls without AMCs. One of the keys would be for banks to have someone inside the institution, who understands appraisals, to help with all these policies and regulations. If you have the training that nearly all our members have, you can tell relatively quickly whether you have something that's logical and reasonable.

We've gone through an era where if you had comments in a report that mentioned condition of a property—

the overall objective of the new regulation is sound. You *do* want to have independence to the appraisal and lending relationship.

The challenge we see now is a shrinking appraiser market. That's because you had appraisers who were working at \$300 a pop, and now are forced to work for maybe half of that, so they leave the appraisal business.

A new barrier is going to make it more difficult. In 2015, there will be a requirement [in Massachusetts; varies by state] that you must have a four-year degree to become an appraiser, and the licensee will be allowed to manage only three appraiser trainees per certified appraiser. You've got an improving market, a decreasing number of appraisers, a higher barrier to entry, and lower fee structure based on AMCs. What does that bode?

Jay Forrester Before coming to this meeting, I asked one of our mortgage folks what question he would ask this group. It was the issue John just mentioned: What are we going to do five years from now when there are no new appraisers coming on board?

Coyle The Appraisal Institute follows this data closely. The number of state-licensed and certified appraisers has fallen significantly over the past five years nationwide. We've gone from more than 100,000 down to about 83,000. The Appraisal Institute represents about 27%-28% of those folks.

Cindy Lowman I don't think we can forget that this is a regulatory issue. It all came about because there was fraud in the mortgage industry and the appraisal industry, so the government got into our business. Because of my bank's size [well under the \$10 billion threshold], I'm fortunate that I can interview and choose my appraisers; I can fire them if I want to. But I still have to do a blind draw. So, I may have one appraiser who's more competent in a particular area that I know will do a really good job, but if that



Lance Coyle



*An unintended consequence:
We've destroyed the relationship
between bankers and appraisers*

things that should be looked at for security of a lending decision, like a bad roof—you'd get calls from the clients saying to take out that comment about the roof. Well, if we did, we'd be violating our professional practice. They shouldn't be asking that, but [the loan] flowed through to the secondary market, where it was off-loaded.

John Brodrick And that really goes back to the root of all this: The conduit for that loan didn't necessarily have skin in the game. The critical component was getting the loan to closing and getting paid. So, I think

Sara Stephens



name is not in the next draw, then I can't send that appraiser.

Borges Are there not some outs on that because of unique circumstances?

Forrester There are some limited outs, but if you take one, you go to the next appraiser in line. So, it's still random.

Stephens The appraisal process has just become a commodity in the single-family venue. We need to get back to the point where we are all working toward the same end. It's not a matter of sending somebody out there who can do it cheap and fast.

Ken Wilson I think the key word is confusion, because I don't know that all bankers, all appraisers, all regulators, and the public truly understand Dodd-Frank. There is a lot of confusion. So, that's part of the problem.

Borges The mortgage industry, especially the single-family world, is driven by a relative handful who, because of their national or very large regional scope, have to rely on a management relationship by an outside vendor.

Lowman But, the rest of us are going to live and die by the rules for those \$10-billion banks.

Do community banks use an AMC?

Forrester We do for residential loans. When Dodd-Frank rules and independence rules came out, and we started using an AMC, there were two significant impacts. One, with the appraisers whom we had long relationships with, and two, with our customers. We had to explain this new fee.

We sell our mortgages in the secondary market, but this Dodd-Frank rule applies to in-house mortgages, too. So, now we have this independence issue for mortgages under \$250,000 that are primary residence Reg. Z loans. We have such a volume that it required adding staff. So, that's another impact.



We need to get back to the point where we are all working toward the same end—not just cheap and fast

Magennis What ends up happening is you have smaller community banks starting to say, "You know, maybe it's not worth us being in this business."

Are AMCs also used for CRE loans?

Magennis We don't use them for taking appraisals. Our chief credit officer actually takes care of that, because he's not on the loan production side, but we do have a review company that reviews each appraisal. The review company is another appraiser.

Forrester We use an AMC for the review after the appraiser is selected. The ordering is set up in credit administration—not loan production—so that meets the firewall test.

Is that new since Dodd-Frank?

Magennis Yes. Before the law passed, I would have called the appraiser and said, for example, "It's a mixed-use property; it's in this town. Do you have experience in that particular market area?" And then I would call two or three people before making my final decision as to who should get the job.

But, I can't have anything to do with that now, so that relationship is gone.

My lenders have no incentive to bring in deals just for the sake of bringing them in. We have a saying at the bank: "It's cradle to grave." So, if you bring in a deal and end up having a problem with it, it's your problem, and you have to handle it.

But on the commercial side, is this arms-length relationship with appraisers a bad thing?

Magennis I have mixed feelings about it. There were occasions where the value came in much higher, and I would call the appraiser and say, "Okay, can you please justify how you came up with this value?" and really understand what was going on in the market. Now, I don't do that, obviously, so a lot of times, I will go to my chief credit officer and say, "Do you have any idea what's going on here? Can you call and find out?" So, you have to do it in a roundabout way that ends up wasting a lot of time.

Brodrick The appraisers who are left are pretty much the cream. We're not



Before Dodd-Frank I would have called the appraiser and asked, 'Do you have experience in that market?' I can't now



Liz Magennis

going to have the problems now that we did earlier, but we're stuck with all this regulation.

EXAM ISSUES

Banks have been pushing back against overzealous examiners who call for reappraisals of properties, with impact on ratings and capital. What are you seeing now, and how are you dealing with the situation?

Forrester In the CRE guidance, only one paragraph deals with the examiners' right to require a reappraisal. So,

there are a lot of options there. The regulators' focus has more to do with the overall risk-management profile of the bank and the risk in its loan portfolio. As a bank, we made the decision several years ago to take a conservative stance and follow the guidance as closely as possible, so I think that's kept us out of some trouble. I think the issue of overzealous examiners is not as big as it was three years ago.

Lowman Correct me if I'm wrong, but one of the things we've seen in the past three or four years is a falling real

estate market. So, the requirement on a commercial portfolio, especially on properties held, is you have to revalue them every few months if you're holding them on the books. I don't know that there's a fault you can put anywhere other than the economy.

Forrester On the impaired loan side, definitely, you have to reevaluate or reappraise at least annually. But the question dealt with an unimpaired loan, a performing loan, or one that might be a watched credit, and having regulators coming in and forcing a reappraisal based on declined real estate values. Guidance clearly says if your primary source of repayment is intact—cash flow from the business—you don't have to.

Magennis There are a lot of variables that play into a reappraisal decision. We've had situations where examiners suggested a reappraisal, but, because we had good comps and we did an impairment analysis on a particular loan, they were okay with that.

Borges I had a conversation with the chief appraiser from a bank recently, and he mentioned regulators seeing an appraisal report that might have a market value opinion in it and a



Because of my bank's size, I'm fortunate I can choose my appraisers, but I still have to do a blind draw



Cindy Lowman

disposition value opinion in it and a liquidation value—all of which are different definitions of value, based on different presumptions. The regulators were requiring writedowns to the lowest value presented in the report. His advice: Ask for the market value. Otherwise, you're digging your own hole.

Forrester I think at the height of the crisis, examiners were struggling to figure out exactly how to apply the [2010] appraisal guidance, and they had a high number of fairly new staff, so they were interpreting some of these rules probably a little more harshly than they needed to.

While this is clearly a bank issue, are there ways that appraisers can assist bankers in addressing it?

Stephens Perhaps it's time for lenders and appraisers to start talking the same talk, or regulators and appraisers to be educated in the kinds of things that they need, that we do.

Borges Market studies could help. That would be one thing that appraisers could do—not an assignment specific to a property, but [their thoughts] about a real estate market on a quarterly basis. You would get information that says, "It sure looks like they're getting too many apartments over on that side of town. Maybe we better not loan 80% on deals over there. Maybe those are 65% deals."

Stephens The optimal: have an appraiser as a part of a bank's staff.

Wilson And if you can't afford that, maybe you could do random reviews. Talk to the appraiser and find out, "How did you arrive at this number?" Because market value is not a finite number. Maybe there is a little more explanation needed.

Magennis Do you all have any recommendations for what young bankers can do to sharpen appraisal skills?

Stephens If someone coming into the business at an entry-level position—or a slightly more seasoned employee—went through the Appraisal Institute's beginning classes and began to understand the principles that are part of the appraisal process and how a capitalization rate is developed, that would be a win. A lot of people coming out of college don't have that background.

Magennis Is class online or in person?

Borges The Appraisal Institute does both. And we're getting ready to start with a synchronous learning program, where you are basically in a classroom on a regular schedule, but the classroom is your desk and the presenter is someplace else. The options are all listed on www.appraisalinstitute.org.

[For information specifically relating to lenders, go to www.appraisalinstitute.org/education/lenders.aspx.]

Regarding in-house appraisers: Do any of you have them?

Forrester We have an in-house real estate group that will either prepare the evaluation or verify the information. But they're not appraisers; they're doing an evaluation. We have considered hiring an appraiser for that role.

Borges I teach both of our general and residential review seminars, and in every one of them, we end up with people who last week were inside the institution—over in the audit department, cash management—and they were trusted, and now they're running



The challenge we see now is a shrinking appraiser market as appraisers are forced to work for maybe half of what they had been



John Brodrick

the appraisal functions. Someone says, “Go take that one-day seminar,” and they’re coming and seeing that you can’t figure this out in one day.

Lowman You have mentioned the lower end of the appraiser group. Do appraisal management companies have top-quality people participating, or is that where you have a concern?

Wilson Designated appraisers are probably on a list, but it becomes a business decision that they are not going to work for that dollar amount.

Borges I’m on some old AMC lists that I haven’t signed up for, and I still get requests [to do appraisals]. I don’t want to work for most of these type AMCs at any fee.

Brodrick And that’s why they reach geographically. They’ll go as far as they need to until somebody says, “Yes.”

APPRAISAL OPTIONS AND SERVICES
When is an automated valuation model (AVM) appropriate? When can you or should you use a broker price opinion (BPO) versus a full appraisal?

Forrester We have determined that we can use an AVM as one tool for evaluation. We never use BPOs—and you can’t use them for an appraisal if it’s a new origination.

Lowman It is really more about when we get to use an AVM, because if it is a HARP [Home Affordable Refinance Program], you can use an AVM, because the agencies say that you can, versus a full appraisal.

Wilson Part of the problem we have with the BPO is it’s exactly what it’s stated to be: a price opinion. It may or may not be equivalent to value. And I think one of the other issues you run into is that it’s from an unregulated industry. Brokers may not have the background and knowledge; they are not subject to the same requirements that appraisers are.

I don’t want to make it appear that I’m down on brokers and BPOs. But, at the same time, there’s a conflict of interest there.

Then the AVM sounds like a more legitimate tool.

Wilson It is, to a degree. But, part of the problem with an AVM is that unless there is some professional input, the models are dealing with public records and information that may or may not be accurate.

Coyle You don’t know that the roof’s been replaced. You don’t know that they added a beautiful flagstone patio in the backyard. AVMs don’t know those things.

Forrester We use it as part of an evaluation for residential properties, but we require a picture to be with it. You can’t just use an AVM and not go look at the property.

Brodrick I think there is more validity for AVMs in an area where the housing is very homogeneous.

Any last thoughts?

Borges The one thing that everyone should take away from this discussion is that a good appraiser should have the *same* opinion of value no matter who the client is. That is the test of a good appraiser.



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Ken Wilson