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Appraisals & Why Andrew Cuomo's Legislation Must Die.

by John Dumke

On May 1st new legislation (by Andrew Cuomo) went into effect, which is crippling the Real Estate market. The piece of legislation that I am referring to is know as the HVCC or Home Valuation Code of Conduct.

Theoretically the intent of the legislation sounded good, to enhance integrity in the appraisal industry. The result however, has crippled a buyers ability to buy a home, created a complete roadblock on many purchases and refinances, and destroyed the careers of thousands of reputable appraisers.

How is the HVCC negatively affecting the market?

The HVCC has prevented lenders from ordering appraisals directly, and from having any communication with that appraiser. Appraisals are now ordered through AMC's (Appraisal Management Companies). When a lender requests an appraisal, an appraisal management company who could be out of Nebraska sends out the next appraiser in the queue. There is no accountability, no feedback, no recourse, and often times, no competency with the appraiser that is next up in the queue.

Couple that with an unknown, inexperienced appraiser that now has to pay 30-40% of his paycheck to the appraisal management company, with homes that now sell for about \$20,000 - \$40,000 more than 3-6 months ago, and it is no wonder that many homes are not appraising.

Previously, an appraisal was just one of the checks and balances in the overall risk profile of a home loan application. Now the appraisal has veto power over whether a transaction goes through or not. Rather than an appraisal confirming that the sales price is in-line or reasonable, now an appraiser is the judge & jury, and his word will now stop a transaction dead in its tracks.

The result of this legislation is that transactions are now highly likely to fall out of escrow due to appraisal problems. I can not state strongly enough that this is single handedly the most devastating rule to negatively affect the Real Estate market. It is my hope that by the time you read this article, the HVCC will be repealed.

Watch this video for a quick overview.

For a quick video overview of the new legislation you can click on www.HVCCPetition.com and click on "HVCC Video".

Last night I personally read through pages and pages of comments on the petition to remove this legislation. I could only feel compassion and pain for the many stories of homeowners unable to refinance, buyers unable to buy homes, Realtors unable to sell homes, and appraisers careers and lives destroyed due to Andrew Cuomo's shortsighted legislation. Personally, I have had three appraisals come in low since the HVCC went into effect.

Before I further get into examples of how the HVCC is not working, let me first talk about the purpose of an appraisal and how the appraisal process has effectively worked over the past 20+ years.

What has traditionally been the purpose of an appraisal?

While most buyers and sellers might think that an appraisal is to determine a homes value, from a lenders prospective, this is only partially true. An appraisal has always been taken in context with the rest of the loan package. The appraisal is only one of many factors that a lender has normally considered when deciding the overall risk when making a loan.

Other important factors are: how much is being put down, what are the buyers credit scores, the buyers debt ratios, the stability of the buyers income, how appealing or how resalable is the property, the condition of the property, how healthy is the overall real estate market, and finally, is it a purchase loan, where a buyer is putting money into the property, or a refinance, where money is being taken out.

All these factors combined *with the appraisal* constitute the overall risk that a lender is likely to experience. The appraisal is just one component to the overall risk of a home loan package. Traditionally, an appraisal has not been a yes or no scenario, simply an independent check to make sure that the value of the home is generally in-line with the other home sales and that the loan package as a whole makes sense.

As simple proof that appraisals have not been for the purpose of determining exact value, I can cite that over the last 20 years about 98% of purchase money appraisals usually come in at sales price. If the homes exact value was truly the answer being sought, then only about 1% of the appraisals would come in at exactly sales price, while the balance would be higher or lower.

Another bit of proof that appraisals have not been for the purpose of determining exact value: Why do refinance appraisals ALWAYS come in low? Because the bank wants to be more conservative when cash is coming out of the property. Is there something wrong with this? I don't think so. Appraisers intentionally come in low to protect the banks interest on a refinance. The purpose of the appraisal in this instance takes into consideration that a lender has more risk when an owner is taking money out of a home.

So then why is the HVCC so bad?

Because the appraisal process is NOT an exact science and was never intended to be incorporated into the loan process as an all or nothing component of the overall risk that prevents or allows and transaction to go through.

Appraisals aren't the true test of value.

While I am not an economist, I believe an economist would say that the true test of value is the price that a willing and able buyer and seller agree upon. The appraiser should be there to just verify that the sales price is "generally" in-line, and this is the way it has always been.

There IS no exact value.

When I am negotiating a transaction with a seller and we get down to the last \$20,000 of value, I really can't say what is the "right" answer. Is a home worth \$560,000 or \$540,000? Most of the time it depends upon whether there are multiple offers and the individual motivation of the buyers that are bidding on the property at that time.

Compare this uncertainty (volatility) to individual stocks on Wall Street. Every day stocks are valued by America's best and brightest analysts, and yet these stock prices may vary by around 2-5% on a daily basis. If stocks vary by this much each day, how the heck is an appraiser going to definitively, say that a homes value is \$525,000. Why not \$545,000. Neither one is right or wrong. When you get down to the last \$20,000 in value, everybody is pretty much in agreement. \$20,000 on a \$500,000 is only 4%. Heck, last year we had swings in the stock market by as much as 10% on a daily basis.

Yet appraisers have been given VETO power over transactions if they come in low and don't agree with what the buyer and seller have agreed upon.

Assuming there is a \$20,000 range of uncertainty and the appraisers averages were perfect, 50% of the appraisals would still come in low.

Exact measurements are stated as a mean plus or minus some range of confidence. It is likely that an exact appraisal for a track home in East Long Beach would have a range of values from different appraisers of around \$20,000 to \$30,000. An appraisal is just an opinion of value. What happens when the half of the appraisals start coming in low? What typically happens is that it shakes the confidence of the buyer. The buyer can proceed if they choose to come up with the difference, but many times they financially can't or their faith is too shaken to move forward.

If the market is going up appraisals come in low.

Appraisals are done looking in the rear view mirror, based upon closed sales that went into escrow up to 8 months ago. Appraisers don't know how to determine an increasing market or a decreasing market. Since when was an appraiser trained like a Wall Street

market technician or a Chartered Financial Analyst that Wall Street employs?

The traditional appraisal form has never allowed for whether the market was increasing or decreasing, but it didn't need to, because as I mentioned 98% of the appraisals came in at value.

Now there is a spot on the appraisal form for whether prices are stable, increasing or declining, and the appraiser can adjust up or down based upon his opinion. Well how the heck does an appraiser from Corona know the exact pulse of the market for 3 bedroom, 2 bath homes in Los Altos that feed into the Minnie Gant Elementary school? They don't. They don't analyze the number of homes sold per month, the rate of change in the number of homes sold per month and the variation between sales prices on closed sales from 6 months ago, versus the current sale prices of pending sales. Combine that with how many homes are on the market, and the caliber of these homes and how they compare to the ones in escrow and what is the current monthly supply of homes. I can guarantee you they DON'T KNOW THESE STATISTICS, and there is NO PLACE on the appraisal form for these type of statistics. Yet based upon one recent appraisal of our listing, some bone head appraiser from Riverside says that a 3 bedroom, 2 bath home in Los Altos will sell for \$18,000 less today. Doesn't he know that there is only a 1.5 month supply of homes on the market and values are about \$20,000 - \$40,000 higher than 6 months ago. No he doesn't.

Most appraisers don't know what they are doing.

My apologies to competent appraisers that are the 10 - 20% of the professionals, but most appraisers don't know what they are doing. In most industries about 10- 20% of the participants are competent and the balance are new, learning, part time or not serious about their profession. Why do you think most businesses fail within 5 years, and appraisers are no different than Real Estate agents, or other professions.

I can't tell you how many times I get calls from appraisers from an area code one hour away, asking me about my listing and what I think about a particular property and its value.

In a free market system, this is self regulating. When an appraiser does poor work, lenders no longer use them. But in Andrew Cuomo's new HVCC world, every appraiser gets the same amount of work, whether they produce quality work or not. Not having any contact with an appraiser might eliminate any influence, but who says influence is bad. Influence and accountability provide the opportunity for lenders to pick the most appropriate person for the job. And right now accountability is non existent.

The appraisal process is a joke.

The standard appraisal form allows for 3 comparable properties. The appraiser is supposed to pick the 3 most appropriate sales, but using only 3 properties is very short sighted. You don't need a PhD. in statistics, to know that when determining averages, and medians, you need large samples. If the typical range for a given type of home in Long Beach is \$100,000, an appraiser can pick 3 properties at the low end or pick three at the high end. The typical appraisal form allows for price to be steered in either direction.

Now after an appraiser has hopefully picked the 3 most appropriate sales (based upon his opinion), these comparable sales have to be adjusted to be comparable to the property being appraised (subject property). This process again is a joke because an

appraiser randomly assigns a value to some difference between the two properties.

Too often, we have problems appraising the highly upgraded properties because a buyer may be willing to pay for extra value, yet the appraiser does not add as much value for the improvement than the buyer would. As an example, we recently had a home with a wonderful 300sf sun room. This room essentially functioned like a family room and would cost around \$40,000 to build, yet the appraiser only gave \$4,000 in value for the addition.

The appraisal process tries to take a highly emotional process and make it scientific, yet I know what sells a home are the emotions that a home offers. This is why it is often the very nice homes that have the hardest times appraising, because a buyer sees value for which an appraiser can't adjust. How is an appraiser supposed to quantify and justify the exact contribution from emotional appeal. They simply can't. I have never seen an appraisal form say, "awkward floor plan", "best model", "Open, light and bright", "weird layout", or "I love this home". But buyers say it all of the time and will discount or pay more for this value.

Appraisal Management Companies are biased towards a declining market and appraisers hands are tied.

There is this preconceived notion that All of California is going down in price, so when appraisals are reviewed, the AMC wants older sales to be adjusted downward to reflect a declining market values, even when prices are actually rising.

Quality of appraisers is way down.

I just got off the phone with a 26+ year veteran appraiser. The kind of guy you can count on for quality work. He said that the typical price paid to an appraiser for a residential appraisal through an AMC is now \$175 - \$195, when he used to be paid \$350 - \$400 per appraisal directly through a lender. Unfortunately the buyer doesn't save this money, in fact a buyers fee for an appraisal has gone up, because there is now a middleman.

With his income being more than cut in half, he says that many veterans have gotten out of the business. Most of the appraisers left simply don't go the extra mile. Quality is not a requirement of AMC's. All they want is the fastest and cheapest appraiser.

Appraisals were never really the problem to begin with.

Market value is set when a buyer and seller come to terms on price, then within 2 weeks the appraisal is performed, after the fact.

What drove prices up too high and encouraged fraud, was 3 years of artificially low rates on loans being offered to buyers that never had a hope of repaying. When money is free for the taking with no risk, (no down payment), fraud will happen.

Trying to control appraisals will not prevent fraud. Preventing unqualified buyers from being enticed into buying a home that they can't afford with no down payment creates fraud.

If down payments were 10% and buyers had to have good credit and income to qualify there would have been no froth in prices or fraud in lending. What buyer would risk his \$50,000 down payment and good credit, by overpaying or other monkey business?

Which leads me to my next point.

The Government should just stay out of the stimulus game.

Free markets eventually have to pay the price for their errors, while the government doesn't seem accountable to anyone.

To create the housing bubble and subsequent credit crunch it took the coordinated help of both the private and public sectors. The Fed kept rates around 1% for 3 years after the dot.com bubble burst, Washington felt that every American should own a home, and Wall Street obliged with free money to all who could fog a glass. Wall Street paid the price, Bear Stearns and Lehman no longer exist. But who holds the government accountable?

In fact the same problem that got us into the mess, financial over stimulus, is the governments proposed solution. This is about as crazy as the drunk who is going to solve their hangover with a little "hair of the dog".

But none the less, the Government steps in with an \$8,000 credit, raised the FHA loan limit from \$427,000 to \$725,000 (which only requires a 3% down payment), and drops interest rates to an unrealistically low rate. Now because loans are so appealing, of course they have to protect the consumer from overpaying.

The government should just stay out of the stimulus game.

As a side note, one appraiser that I just spoke to mentioned he just qualified for a government grant to help his daughter go to college, because his income was more than cut in half. Never in his wildest dreams did he ever figure that he would qualify for this type of government economic assistance.

Doesn't this just sound a little socialist? Appraisal fees go up, so that the government can protect buyers. The reality is that buyers no longer can purchase homes, because properties no longer appraise. An appraiser's business model is taken from him and given to somebody else to insure government oversight, but now this appraiser qualifies for federal financial assistance.

The government does not know how to best allocate capital. I thought this was proven with the fall of Russia?

Experienced veteran appraisers are the biggest losers.

While I might complain about a few homes that I now have to re-sell due to a low appraisal, at least my business of helping clients is still intact. Not so for appraisers. They have been robbed of their livelihood, and what has happened to them is simply un-American.

Imagine if you were a seasoned professional appraiser with 20+ years in the industry. You spent the last 20 years cultivating valuable relationships with lenders that trusted and counted on your competent work. These relationships might represent \$100,000 or \$200,000 of annual income, your bread and butter, and you treat them like gold. You are conscientious, timely and accurate.

Now Andrew Cuomo decides that you can't work directly for your clients. In fact, it is now ILLEGAL for you to solicit their business. On top of that, your only source of business is to put your name in the queue with an Appraisal Management Company.

And for the privilege of getting assigned a small portion of the business that you once earned and cultivated by your own sweat, you now have to pay the AMC a 30-40% referral fee. Imagine if the Government, dictated that you could no longer work directly with your clients and you had to pay a 30-40% referral to a middleman, who determined how much work you would receive.

To me this just sounds wrong and I am appalled that this could happen and you should be as well.

Please go to www.HVCCPetition.com and sign to have the HVCC legislation permanently repealed. This is the Greatest Debacle I have see in the legal workings of Real Estate since the No down, stated income loan to buyers with bad credit.

REAL ESTATE NEWS

Inside.....

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Los Altos - 1873 Iroquois

3 bedroom, 2 bath, 2,292sf., spacious, open and contemporary, new int & ext paint.
\$649,000 [More photos online](#)



La Marina Estates - 1401 Iroquois

4 bedroom, 2 bath, 2,372sf, on a large 7,150sf lot. New paint and flooring.
\$675,000 [More photos online](#)



Los Altos - 2163 Charlemagne

2 bedroom, 1 bath, plus a 1 bedroom, 1 bath guest house & RV parking.
\$475,000 [More photos online](#)



Los Altos - 1824 Hackett

3 bedroom, 1.75 bath, 1402sf., extensively remodeled.
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