

APPRAISAL MODERNIZATION

– A DATA RETROSPECTIVE



BY ELIZABETH GREEN

A residential appraisal report is scrutinized by more parties than any other document in the mortgage loan origination process. Further, it is the only document prepared by a licensed professional who has personal legal liability for the work product. The primary reason for such attention is that the property value is the lynch pin in the mortgage transaction balancing the Loan to Value (LTV) ratio.

Appraisers deliver conclusions in writing for a wide variety of intended uses and users. In fact, a

professional appraiser can deliver his opinion of value in any form or format, including the back of a napkin. Today's Uniform Standards of Appraisal Practice (USPAP) is an ethics standard that dictates how the appraiser arrives at conclusions, not necessarily how he delivers them. Historically, it is the client paying for the appraisal service that dictates the format and content of the requested analysis, definition of value, and the content of the report.

The report templates in use today were originally designed in the early 1970's to collect and present data in the pre-digital age. Detailed facts about the subject property, neighborhood, and market could only be obtained through local professionals. The first evidence of uniformity began to take shape in 1940 when the Society of Real Estate Appraisers adopted a code of ethics. In 1946, the Federal Housing Authority (FHA) issued the first appraisal manual and the Savings and Loan (S&Ls) industry of the 1960's began to drive not only a reporting standard, but to hone the definition of value that would shape the role of appraisal in mortgage banking for years to come. S&Ls accounted for 90% of the mortgage originations in the 60's and 70's. Homeownership rose from 43.6% in 1940 to 64% by 1980 due to the federal program introduced with the New Deal in the 1930's.

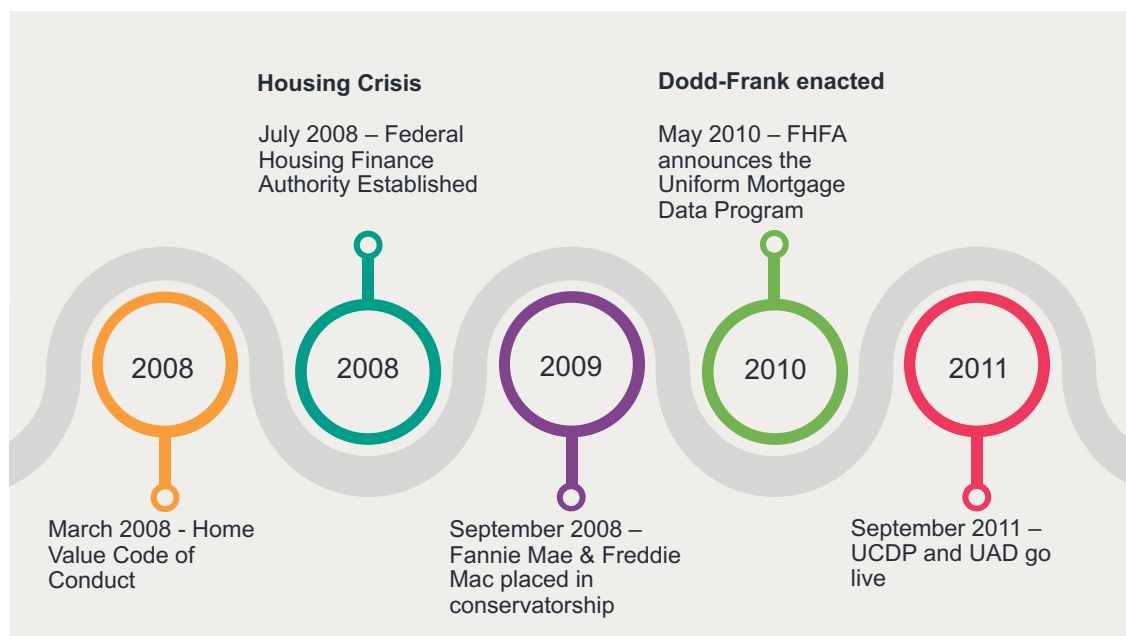
Electronic word processing in the 1980's displaced the typewriter. Digital cameras replaced Polaroid photos. PDF compression and email displaced the courier. Fast-forward through the boom and bust of the 2000's to the intervention of the federal government in 2010 with the Dodd-Frank Act, the stage was set for change. Some new initiatives were successful, like appraisal independence measures. Others, like Reasonable and Customary Fees, fell short. In 2011, with the implementation of the Uniform Appraisal Dataset (UAD) and the Collateral Data

Portal (UCDP), appraisals for loans sold to Fannie Mae or Freddie Mac (the GSEs) are delivered as machine-readable data.

Since 2011, data from 31 million appraisal reports - and counting, are now in databases controlled by Fannie Mae and Freddie Mac. This includes appraisals for loans that don't close, loans that are not ultimately purchased by a GSE (but were shopped to them), and any appraisal revisions (up to three copies of an appraisal can be "on file" per transaction).

One of the most interesting derivative technologies, specific to appraisal, that has been developed from UAD data, is the Fannie Mae Collateral Underwriter and Freddie Mac Loan Collateral Advisor.

These decisioning platforms allow a lender to analyze collateral risk by comparing the uploaded appraisal to the data and analytics driven by UAD data collection. The proprietary output and scores are shared only with the lender. The ongoing, cumulative UAD data is not only applied to check the information submitted on new appraisals in the UCDP, it is also leveraged by the respective Automated Valuation Models (AVMs) that each GSE has developed which in turn plays a role in their respective automated underwriting platforms.



MODERNIZATION

The GSEs continue to develop policies and processes using UAD data. Currently, there are several different “modernization” activities in play or under development and many will result in limiting the role of the professional, licensed appraiser.

APPRAISAL WAIVERS

Originally known as a Property Inspection Waiver. This option is available to lenders for certain qualified transactions and is offered using Collateral Underwriter powered by data and analytics.

When a transaction is not eligible for a waiver, Fannie Mae envisions an evolutionary process that cascades to the level of collateral risk assessment product that fits the need of the subject property.

PROPERTY CONDITION REPORTS (PCD)

This is a new class of inspection. Only products may

be sourced from a variety of sources and would be submitted and analyzed against the massive collateral GSE databases.

If the PCD alone is not enough for the collateral risk assessment, the PCD could be provided to an appraiser. It is important to note that the PCD data, when given to an appraiser, is considered to be like any information provided by third parties, such as flood assessments. Ultimately, the appraiser must decide if the information will be relied upon in an ensuing appraisal report. USPAP is engaged and liability applies.

BIFURCATED/HYBRID APPRAISAL REPORTS

Pilot programs with the GSEs have been underway with different types of inspection data sources, combined with valuation tools and appraisers, to essentially perform desktop valuations.

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UAD2

New XML Dataset requirements – the published materials from the GSEs on this topic indicate they are looking to move up to a current MISMO version and will most likely instigate a new version. It's important to note that the current UAD requirements were reconciled into MISMO version 3.3, which was published as a final recommendation in February 2017. The current MISMO published version is 3.5.

A key area of interest for UAD2 is support of all property types, and of particular interest, is the appraisal requirements for 2-4 family properties currently supported on the IO25 -- Small Residential Income Property Appraisal (used for appraisals of two to four-unit properties) and the IO07 -- Comparable Rent Schedule Addendum (used to estimate the market rent of the subject property).

NEW APPRAISAL FORMS

The buzz word here is "dynamic" and "user-friendly." Based on the Consumer Financial Protection Bureau's Closing Disclosure (CD), the GSEs see the benefit of only displaying data that is relevant to the transaction. For a CD, this means not presenting purchase-related information on a refinance transaction. However, a dynamic form is not as "cut and dried" for an appraisal. This is primarily due to the definition of appraisal in accordance with current USPAP. The appraiser must decide what is relevant to include and is liable accordingly. Even the current GSE Seller/Service guidelines indicate that while the forms are required,

the appraiser must include all information, addenda, etc. beyond the form to support his conclusion of market value. The appraisal process must collect all the information first to determine what data is relevant for the appraisal report for the given subject property.

Since the recovery began and the GSEs went into conservatorship, their mandates from the regulator have been carried out in the form of technological advancements in all areas of their businesses. Many of these appear to be part of a longer-term strategy – maybe one that may be the key to an exit strategy from conservatorship. The Common Security initiative holds the key to the GSEs future, perhaps foretelling a move from their role as creator of mortgage-backed securities to one of being a user on a utility platform that facilitates the issuance of mortgage-backed securities (MBS) with other participants holding the market risk. The Uniform Mortgage-backed Security was launched on June 3, 2019.

The question that must continue to be asked is how will these changes deliver a better, more reliable valuation?

It is extremely important for appraisers, lenders, AMCs, etc. to stay well informed about the changes and activities being advanced by the GSEs in the realm of collateral risk assessment. Seek out opportunities to get involved and be a part of these changes in a positive and impactful way. The appraisal profession is changing. Now is the time for the profession to step up and define its future.



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Elizabeth Green is Chief Collateral Officer at LoanLogics. In this role, she is responsible for the expansion of the company's product offerings in the area of collateral risk assessment and developing the overall product strategy for these solutions. Elizabeth is a strategist, solutions architect, speaker, and valuation advocate. As a recognized mortgage technology veteran in software product leadership for solutions in residential property valuation, loan origination, mortgage servicing, and secondary marketing, she has helped to foster a new level of understanding in property valuation and collateral risk assessment through the application of digital intelligence. A 25-year veteran leader in the mortgage software and valuation sectors. Elizabeth has led the MISMO Property and Valuation Services Group for the last 10 years and has been instrumental in defining and establishing standard terminology and definitions for this sector.