Raising the appraisal threshold: Does this make sense? by Bill Pastuszek

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Bill Pastuszek,
Shepherd Associates

You may well have heard about this change. This was mentioned in a 2018 article. Here's some information.

From the Federal Register, Vol. 83, No. 235, Friday, December 7, 2018: "The proposed rule would increase the threshold level at or below which appraisals would not be required for residential real estate-related transactions from $250,000 to $400,000." With me so far?

Further, "Consistent with the requirement for other transactions that fall below applicable thresholds, regulated institutions would be required to obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices." What is an evaluation, you may ask? It's a valuation service that does not require compliance with USPAP or the signature of a credentialed appraiser. Making sense?

Question: Didn't we just–reasonably recently, anyway–get over the Great Real Estate Recession which hammered residential markets and spurred major reforms to the residential lending industry? Wasn't one of the signal lessons learned from that extended debacle to maintain a strong appraisal process?

Two years ago, something called the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA) asked and answered the question. The review by the agencies, concluded that "Based on considerations of safety and soundness and consumer protection, the agencies do not currently believe that a change to the current $250,000 threshold for residential mortgage loans would be appropriate. Further, "The agencies will continue to consider possibilities for relieving burden related to appraisals for residential mortgage loans, such as coordination of our rules with the practices of HUD, the GSEs, and other federal entities in the residential real estate market." What a reasonable approach to a somewhat complex problem.

The Appraisal Foundation (TAF) voiced its opposition as follows: "We believe that this is contrary to basic principles of safety and soundness as well as consumer protection." TAF goes on to say that with "systematic" "carved out" appraisal exemptions in Title XI of FIRREA since its 1989 inception, the current proposal would exempt over 90% of residential mortgage transactions. The letter goes on to say that the chair of the House Financial Services Committee is a proponent of appraisals from the consumer protection perspective and the issue would likely be raised in committee.

What does this mean for the market? The last crash stemmed at least in part from loose lending practices which included drive-by appraisals, pressure on appraisals, selection of incompetent appraiser, and poor–or non-existent–review practices. Legislative changes created greater appraiser independence and GSEs create means for better market analysis and documented support for opinions in appraisals.

As memory fades about the last downturn, market participants are once again setting their sights on their big problem: The appraisal (& appraisers).

Why now? Most markets – certainly here in the Boston Metro – have experienced a very positive period of strong demand and low inventory. Appraisers for the most part have shown integrity, competence, and resistance to undue influence.

Is there a shortage of appraisers? There is little compelling evidence to suggest there is, especially at this down side of the cycle. During the hottest parts of the market, there was a shortage of all real estate professionals, inspectors, surveys, examiners, not just appraisers.

Are appraisals too expensive? Ken Harney, the columnist, notes that the appraisal is one of the least expensive parts in a transaction and states that "on a $350,000 home purchase, a $500 appraisal represents 0.0014% of the cost. For a home buyer, a professional opinion of value serves as a check on whether the house is priced too high."

Is this a way to lessen the important influence an independent objective appraisal process has on residential markets? Think about it. What might just happen if the moderating influence of appraisers is removed or diminished?

Consider this. The change represents a clear opportunity for technology-driven valuation services to leapfrog traditional appraisals which represent effective risk management tools.

Does this advance consumer protection? It would seem to retard or reverse it. Does this change promote sound banking practices? Hard to see why it would.

Final question. The current system is not broken, so why does it need fixing? More on evaluations in a follow up article.

You had until February 5th to comment, according to the Federal Register. By the time this article goes out, that time has come and gone. The websites of The Appraisal Institute, American Society of Appraisers, and MBREA contain helpful information to aid you in making your opinion heard.

An email or call to your state and Washington-based legislators would be helpful. In my opinion, this issue is far from settled.

Bill Pastuszek, MAI, ASA, MRA, heads Shepherd Associates, Newton, Mass.