CRN

Collateral Risk Network, Inc.

Best Practices for Fee Panel Management

Introduction

Much of the post Mortgage Crisis housing finance guidance on the subject of appraiser selection has been in harmony. The fundamental challenge for lenders and their agents is in merging all of the many regulations and guidance around this topic to implement a single coherent and consistent policy. The objective, once the policy is in place, is setting policy into motion with a “best practices” approach.

The significance of selecting the appropriate appraiser for each assignment cannot be overstated. According to the late Robert L. Parson, who was the Appraisal Policy Specialist at the Office of the Comptroller of the Currency (OCC) “appraiser selection is the single most important part of the appraisal process. Nothing trumps it”. Lenders and their agents should be giving serious consideration to how they initially select their appraiser and how they continuously monitor them. It is a two-step process.

An honest, competent appraiser produces a credible appraisal report. The purpose of engaging a fully vetted appraiser is to avoid certain risks—compliance risk, operational risk, repurchase risk, default risk, and lawsuits from investors as well as borrowers. It is also, simply put, the right thing to do.

Best Practices Approach

The objective of this white paper is to pull all of the regulations and guidance together in a unified document and build a best practices approach. As with other areas of guidance, the regulators generally avoid a checklist approach. Our “best practices” however takes a holistic view of the topic at hand to provide a clear road map. While every effort was made to examine and analyze all the regulations, guidance and commentary specific to this subject, this document is not intended to serve as a substitute for legal advice.

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Fee Panel Management

Definition

The process by which a lender (or their agent) engages an independent appraiser. Implicit in this process is the initial vetting to select an appraiser as well as ongoing monitoring.

There are several ways a lender can manage a fee panel:

1. Directly engage
2. Engage a third party (AMCs)
3. Incorporate a staff model
4. Hybrid-- both direct and use of third parties or a blend with staff

Any and all of these options can be managed with a “best practices” approach. If a lender chooses to outsource any or all of its appraisal function, they are increasing their risk. This will require additional oversight by the lender or their third parties. A risk/cost analysis should be carefully developed. Maintaining staff is considered by some to be the best path for achieving quality and meeting service metrics. This plan too requires a high degree of resources to manage. A financial institution cannot abdicate their responsibilities of the appraiser selection process to a third party.

A lender can ensure that they are in compliance by developing their own fee panel and defining the scope of work for the AMC to manage the order fulfillment process and quality control. Or they can audit the appraiser selection process of their third parties. AMCs must be completely transparent with their panels in order to ensure that all parties are compliant.

There are a number of panels that a lender or their third parties should manage. Implicit in the guidance is the management of both exclusionary and approved lists. Some choose to also manage a “watch” list or “probationary” list. Once you have completed the vetting of an appraiser, logic would dictate that you would move them to either an approved or “do not use” list. If they fall into a probationary list, there must be a written policy with guidance as to how and when they get moved to another list. All fee panel criteria must have written policy.

Summary of Best practices for Fee Panel Management

- Know your vendors
- Your vendor manager is a key employee
- Ensure you are paying C&R
- Maintain clear policy, easily accessible
- Audit your third parties. Include site visits. Constantly monitor
- Survey appraisers and ask them how you are doing
- Have a mission statement: "Engage the best and compensate them fairly"
- Create a profile and attach to each report

Cost Vs. Fees

If it is generally understood you cannot achieve a cheap price, outstanding quality, and quick service, why do we insist that appraising is the exception to the rule? There have been a number of business school papers written on this generally accepted principle. Even if you could defy the gravitational pull of business rules, the guidance on this issue is quite clear, you may not place service or fee before quality.

With this discussion, the executives of any appraisal department need to consider the actual cost, not the fee, of an appraisal. Factors that must be considered include:

- Repurchase risk
- Revisions
- E&O Claims
- Lawsuits
- Compliance risk—MRAs (Matters Requiring Attention)

Price

- Look to the Dodd Frank Act for guidance on how to establish a fee schedule for payment of a “Customary & Reasonable” fee.
- Ensure you are not withholding payment and violate appraisal independence.
- Pay a fair fee in a timely manner.
- Cheap is ultimately very costly. It is transference of wealth to your legal team.

Service

- What is a reasonable turn time?
- Why not order the appraisal earlier in the process?
- Why not collect information about the collateral at the time of application?
- How do you measure professionalism?
- Do you have policy on attire?
- Do you have policy on proper communication?
- Do you survey your appraisers to find out how you are doing with service?

Quality

- You will know it when you see it.
- Automated QC systems identify non-conforming properties.
- AVMs don’t do a great job of selecting the best comparable sales.
- It is not a great idea to suggest that appraisers respond to an AVM.
- Good appraisers produce credible appraisal reports.

It is often asserted that increasing fees paid to appraisers will not magically make them better appraisers. That is true. But you will also not be attracting the right appraisers onto your panel if your fees are unacceptable. You only can consistently achieve quality when you pay a fair fee. As a profession we will never attract the next generation of well—trained, well-educated appraisers if we continue efforts to compress fees.

Developing a solid fee panel is a lot of work. The investment on the front end of the process will be the defining moment in setting the relationships you maintain with your panel. Appraiser selection best practices will indeed separate a successful appraisal program from one that is not sustainable. Taking advantage of vendors in periods of low demand is not a best practice or a viable long-term strategy.

Policy

Having written policy is a requirement. Bank examiners look for, not only written policy, but an assurance that policy is actually practiced. Conversely having best practices without underlying policy is also insufficient. The old adage “say what you mean, mean what you say” works well for regulatory compliance.

For the onboarding process, written policy needs to address the following:

- Selection criteria
- Application process
- Master Engagement Letters
- Background screening of professional records
- Professional conduct
- E&O insurance
- Independent contractor vs. Employee status

For the maintenance of your panel, you should have written policy for:

- Committee composition
- Process for removals, additions and rebuttals
- Reports to States and other agencies
- Letters for written notification

Guidance demands both initial vetting and constant monitoring. Constant monitoring would include written policy on:

- Background checks
- Disciplinary history
- Review
- Scoring-- turn times, professional conduct, quality, revision request frequency

Master Engagement

Master engagement letters have been a source of consternation for the appraisal community. While some clients have ignored them altogether and just relied upon an order form, others have chosen the completely opposite path of drafting an engagement letter of twenty plus pages. A simple order form referencing the master engagement letter keeps a concise process for each order. As for a best practices approach, keep the Master Engagement letter simple.

The purpose of a master agreement serves to memorialize terms and expectations. If there are any disputes the process is outlined in advance. Well managed expectations make for a mutually beneficial professional relationship.

Items that should be addressed in a Master Engagement letter should include:

- Reference to policies and where they may be accessed
- Insurance
- Application
- Background checks
- Disciplinary policy
- Professional conduct
- Reference to payment schedules
- Dispute resolution process
- Confidentiality statement

What should NOT be in a master engagement letter:

- Inappropriate indemnity agreements stating that the appraiser is responsible for things beyond their control (see State laws)
- Keep it brief. 20 plus pages of legalese is not the way to establish mutual trust
- HVCC certification or a statement that the appraiser certifies that the appraisal was ordered in an AIR compliant manner
- Statement that the fee they accept is C&R
- Insurance requirements that are too high

Each appraiser engaged should sign a Master Engagement Agreement. Each appraiser must be individually vetted and monitored. All of these expectations should be included in the Engagement Letter.

Insurance & Risk

Errors and Omissions insurance (E&O) provides for the worst-case scenario where the AMC or lender is suing the appraiser for negligence in performing an appraisal. Just the request for the appraiser to maintain E&O is, in and of itself, an excellent self-screening process. Appraisers who have an active claims history generally cannot obtain insurance. The lack of a requirement acts as a magnet to attract appraisers who are high risk.

Regulatory guidance generally requires lenders to analyze the risks posed by third party service providers and consider the appropriate types of insurance to be required (but the guidance states no specific requirement). The OCC guidance, per Bulletin 2013-29, advises that banks should require a third-party service provider to maintain adequate insurance, notify the bank of material changes to coverage, and **provide evidence** of coverage where appropriate.

The bulletin advises that banks should consider the applicability of “fidelity bond coverage, liability coverage, hazard insurance, and intellectual property insurance.” Of these types of coverage, the most relevant to a lender/AMC with respect to an appraiser is **professional liability and general liability insurance.**

Professional liability is the most relevant coverage for appraisers because it covers the appraiser for negligence in the performance of an appraisal causing financial harm (e.g., the appraiser is sued for negligently high appraisal that leads the lender to make a loan at too high of an LTV that it would not have made except for the high appraisal). General liability is of lesser relevance to actual claims involving appraisers (but costs an appraiser less because of that fact) and covers the appraiser against claims for personal injuries, bodily injuries and property damage caused by the appraiser.

Insurance requirements as stated in policy should include:

- $300,000 per claim and $600,000 aggregate. Higher property value states-- $500,000 per claim and $1,000,000 aggregate.
- Require proof of insurance in the form of a Certificate of Insurance (30 day notice of cancellation) to the lender/AMC.

- “Prior Acts”-- date matches the time of first performance of services for the lender/AMC and that the appraiser does not make a change resulting in loss of that prior acts coverage.
- “Claims Made” -- claims are not made for a long period of time after the date of an appraisal, it’s important to consider a requirement that the appraiser keep in place professional liability insurance for a certain period of time even after the agreement with the lender/AMC ends.

Peter Christensen, general counsel for Liability Insurance Administrators, suggests language for your Master Engagement letter:

Professional Liability (E&O) Insurance

Appraiser shall at all times during the Term of this Agreement maintain professional liability insurance (“E&O Insurance”) covering damages arising from the professional appraisal services delivered by Appraiser under this Agreement. Appraiser’s E&O Insurance shall: (i) have a minimum liability limit of [$300,000 or $500,000] per claim and [$600,000 or $1,000,000] in aggregate for all claims, and (ii) be issued by an insurance carrier having a Best’s Financial Strength rating of A-- or better. The E&O Insurance policy shall not contain a “regulatory agency exclusion” or any other exclusion for defense or damages relating to claims arising out of failed financial institutions or claims made by the Federal Deposit Insurance Corporation or any other state or federal regulator or insurer of banks, mortgage lenders or other financial institutions.

No later than the date of first performance of services under this Agreement, Appraiser shall have its E&O Insurance provider provide a certificate of insurance coverage evidencing Appraiser’s current E&O Insurance and providing for 30 days advance notice of cancellation or termination of the E&O Insurance to to [AMC] or [AMC’s] designated risk manager. Appraiser shall have such certificates of insurance issued to [AMC] for each annual renewal of Appraiser’s E&O Insurance during the Term of this Agreement. During the Term of this Agreement, Appraiser may change its insurance carriers providing E&O Insurance, but shall not obtain coverage from a carrier or under an insurance policy which results in the loss of prior acts or retroactive date coverage covering the dates on which assignments were performed under this Agreement. Appraiser shall continue to maintain the E&O Insurance coverage required in this section, either by continuation of similar coverage with the same or a different insurance carrier or by the purchase of extended reporting period coverage or “tail coverage,” for a period of three years after the date of completion of Appraiser’s last assignment under this Agreement.

Commercial General Liability (or CGL)

During the Term of this Agreement, Appraiser shall maintain commercial general liability insurance on an occurrence basis covering bodily injury, property damage liability, and personal and advertising injuries. The policy must provide coverage for [Lender/AMC] as an additional insured and waive any rights of subrogation against [Lender/AMC]. The policy must be primary to, and without contribution from, any insurance maintained by [Lender/AMC] and shall have a limit of not less than [$500,000 or $1,000,000] per occurrence.

Other important risk mitigation activities should include questions posed during the application process to help weed out problem candidates. Often, but not always, an appraiser, will self-select themselves out of the process when E&O and criminal background checks are mandated.

Some lenders are requiring that the panel management process include an examination of the employment status of the appraiser. If the appraiser is engaged as a 1099 (independent contractor) by a firm, the firm is functionally an AMC, or third party, masquerading as an appraisal company. The risk this brings to the lender, if they use AMCs, is that the AMC is engaging yet another third party. There are many risk factors when a third party engages yet another third party including but not limited to compliance with C&R.

Appraiser Selection Criteria

The guidance is abundantly clear on this subject—appraiser qualifications must come before fee and service considerations. What is not explicit in the guidance is the criteria by which you should base your engagement decision. Here is a checklist of criteria to consider:

- ASC.GOV verification
- Education
- MLS or other local data sources
- Identity verification
- E&O insurance
- Foreign languages
- Minority & Women Owned Business
- Sample appraisal reports
- Competency Exams
- Scoring
- IC vs. employee (1099 or W2)
- Fee schedules
- Areas of expertise
- Geographic coverage
- Photo of Appraiser
- Signed Master Engagement Letter
- References
- Background screening--disciplinary actions and criminal checks
- Turn times

Competence might be the most difficult to assess. Best practices would indicate that requiring competency exams on each area of expertise, along with an examination of the education in a given specialty would be warranted as well. Do they have the proper credentials, for example, to accept a complex assignment? Sample appraisals are another method of ensuring competence.

Samples by definition should represent an appraiser's best work. Some appraisers refuse to produce samples stating a USPAP violation. USPAP provides an FAQ on the matter. An appraiser has 3 options:

1) Seek permission from the client
2) Redact confidential information
3) Refuse to comply with the client request

The third option, like background screening and E&O requirements, are self-selection methods that are exceedingly efficient. It is always preferable to discover these objections before engagement.

Geographic competence is a buzzword often used as of late. There have been some practices whereby the cheapest appraiser, not the best appraiser, is engaged but is not located in the local market. Please note proximity to the subject does not denote competence and conversely distance from the subject does not imply incompetence. The application of some common sense and proper due diligence will reveal the best choice. One important bit of data to seek is whether or not the appraiser has access to local MLS in the subject market or an inquiry into how many reports they have prepared in that market over the past 12 months.

Understanding Background Screening

A **background screening** or **background investigation** is the process of looking up and compiling criminal records, commercial records, business practices and financial records of an individual or an organization. Background screening is not synonymous with criminal background checks. Screening is a much broader term. Background screening is often a means to objectively evaluate a person's qualifications, character and fitness. It is also the path for the initial vetting stage of appraiser selection.

There are several flavors of screening:

- Criminal background checks --7 to 10 years
- Professional license history/disciplinary records
- Civil searched- done at the county court house level
- Employment references

Criminal Background Checks

There are several reasons for performing criminal background checks. First, there is risk management. No lender wishes to place their customers in harm's way. The appraiser, from the consumer's perspective is representing the lender.

It is imperative that they present themselves in a professional manner and have reputable credentials as well. Background checks are fairly inexpensive to run. The party ordering background checks must adhere to stringent Fair Credit Reporting Act laws. There are also State laws surrounding background checks. Some States allow for a 10 year history, others a 7 year history.

Some criminal background checks include fingerprints. This would be a requirement that would yield no perceivable lift in information, yet would serve to create barriers for the appraiser. An appraiser who is licensed in multiple States would have to submit to fingerprints in each jurisdiction. Fingerprints take a considerable period of time to verify, approximately 2 weeks, while instantaneous criminal checks can be done against national databases.

The CRN recommends the following criminal background check as an industry standard:

- Arrest records
- National Criminal Search
- Terrorist Watch List
- Office of Foreign Asset Control (OFAC)
- Social Security Trace
- Federal District Criminal Search
- Sex Offender Registry

Disciplinary Actions

A check of the www.asc.gov registry will reveal the following:

- Voluntary Surrender
- Suspensions
- Revocations

Only suspensions that are currently in effect appear in the registry. Prior suspensions do not appear in the ASC registry. The States have created their own disciplinary actions that remain under the radar and do not appear in the ASC registry. These are labeled censure, admonishment, education and so on. It would be necessary to inquire with the State agency for each and every appraiser on a periodic basis. The ASC registry will only serve to verify status of the credentials but will not necessarily reveal any underlying consent orders. A check of the ASC registry is just a small step in the overall process of due diligence.

No client wishes to suffer a repurchase demand and discover after the fact that the appraiser has a history of disciplinary actions suggesting incompetence. While there is no explicit requirement for criminal background checks or an examination of disciplinary records, a best practices approach would dictate both of these as essential when choosing the best appraiser for an assignment.

Lenders have been reporting that the FFIEC regulators have been issuing MRA (Matters Requiring Attention) for not performing proper “reputation screening”. This is aligned with Bob Parson’s statement that “appraiser selection is the single most important part of the appraisal process”. Proper screening would include both criminal background checks as well as disciplinary records checks with each State appraisal agency.

Appraiser selection based upon sensitive personal and professional screening should not be offloaded to a third-party background check provider. It could also potentially not be compliant with FCRA (Fair Credit Reporting Act). There are a growing number of FCRA related lawsuits each year.

Managing Panels

There is nothing explicit in the guidance, which suggests that you must maintain a panel. But common sense and adherence to a best practices approach would dictate that you must. Once an appraiser is properly vetted, they should be placed upon an “Approved” list otherwise you will have to perform a lengthy process for each and every order.

Conversely, if an appraiser has performed poorly, caused losses due to over valuation, committed fraud, or triggered repurchase requests as a result of errors or omissions, it would be prudent to place them on an “Exclusionary” list. Some lenders and AMCs also manage a “Watch” list. This list can be for new panel members or for those who are having challenges meeting service levels.

Unfortunately, “blacklisting” has negative connotations and inspires fear among appraisers. The practice of removing appraisers from a panel, for all the wrong reasons, has been horribly abused. A best practice would be to abandon any lists from the pre- HVCC era if the provenance of that list has not been documented.

Dodd Frank mandates that lenders and AMCs must file a complaint for substantive USPAP violations. It would stand to reason when a complaint is filed that the appraiser would automatically be placed on a DNU (Do Not Use) list. The practice of managing exclusionary lists, in a responsible manner, is a must.

Many lenders and AMCs manage their fee panels by committee. A committee format would be comprised of staff appraisers, with an understanding of USPAP, and relieve any single individual from making a potentially career ending decision about a fee appraiser. Management by committee, with a solid rebuttal process, ensures that all parties engage in a transparent, fair process.

Here is what FHA says about establishing Do-Not-Use lists:

Allowing the removal of an appraiser from a list of qualified appraisers or the addition of an appraiser to an exclusionary list of qualified appraisers, used by any entity, without prompt written notice to such appraiser, which notice shall include written evidence of the appraiser's illegal conduct, a violation of the Uniform Standards of Professional Appraisal Practice (USPAP) or state licensing standards, improper or unprofessional behavior or other substantive reason for removal.

While there is no federal law that mandates that an appraiser be notified of removal from a panel, there are some State laws that do require notification. It would be a best practice to have this policy clearly available and accessible to appraisers with a rebuttal process.

Fannie Mae and Freddie Mac also maintain exclusionary and watch lists, of sorts. These lists also cannot be obtained directly by AMCs. Lenders need to maintain a process to inform their third parties, in real time, of changes to these lists. Both policy and process are critical with respect to managing lists. At all costs, appraiser independence must be at the core of fair and equitable fee panel management.

Customary & Reasonable Fees

This is by far one of the most challenging components of fee panel management. Let's first examine what are immutable facts… fee cannot be the determining factor in appraiser selection. Payment of a "Customary & Reasonable" fee is a matter of federal law. Dodd Frank outlines the process of determining C&R as follows:

Lenders and their agents shall compensate fee appraisers at a rate that is customary and reasonable for appraisal services performed in the market area of the property being appraised. Evidence for such fees may be established by objective third--party information, such as government agency fee schedules, academic studies, and independent private sector surveys. ***Fee studies shall exclude assignments ordered by known appraisal management companies.***

The Interim Final Rule introduces two "Presumptions of Compliance" that directly contradict the law. While there is nothing to prohibit anyone from adopting either presumption it would be considered a best practice to adhere to the language in the law. To do otherwise would put the lender and their agents at risk. Litigation is costly. And taking an adversarial position against the appraisal community would not be a sustainable long- term strategy. It is simply the compliant thing to do and the right thing to do to engage the best appraiser and pay them a fair fee.

Once a financial institution has established their policies around C&R, it is a matter of determining a fee schedule. The lender should be establishing a fee schedule by which their third parties should engage appraisers. To adhere to a best practice approach the lender should negotiate fees for service based upon scope of work with their third parties. Some lenders may choose an AMC to simply engage and place orders while others may want a thorough documented QC process. There is an entire spectrum of services that third party AMCs can offer. Like any other business, the fee and the scope need to be aligned for a mutually beneficial relationship.

The development of a national fee schedule is fairly straightforward. It really isn't complicated. Create a spreadsheet with each county and each product in the US. Dodd Frank states that you may use the following methods—independent fee survey academic studies or a government fee schedule. A solid plan might be to examine all three methods. Fee surveys can be sent to your current panel as well as to the entire population inexpensively. Several States now have academic studies available. When in doubt you can always default to the VA fee schedule.

Mandatory Reporting

Reporting an appraiser to their state appraisal agency for violations of USPAP has always been a requirement. Dodd Frank merely reinforced the practice with the full weight of a federal law. The GSEs also require that a lender file a complaint when it is discovered that the appraiser violated State laws or behaved unethically.

Dodd Frank Mandatory Reporting:

Examples of material failures to comply

- *Materially mischaracterizing the value of the consumer's principal dwelling, in violation of § 226.42(c)(2),*
- *Performing an appraisal in a grossly negligent manner, in violation of a USPAP rule*
- *Accepting an appraisal assignment on the condition that the appraiser will assign a value equal to or greater than the purchase price to the consumer's principal dwelling, in violation of a USPAP rule.*

Interagency Guidelines:

- *An institution should file a complaint with the appropriate state appraiser regulatory officials when it suspects that a state certified or licensed appraiser failed to comply with USPAP, applicable state laws, or engaged in other unethical or unprofessional conduct.*

- *An institution must file a complaint with the appropriate state appraiser certifying and licensing agency under certain circumstances. An institution also must file a suspicious activity report (SAR) with the Financial Crimes Enforcement Network of the Department of the Treasury (FinCEN) when suspecting fraud or identifying other transactions meeting the SAR filing criteria.*

GSEs:

- **Freddie Mac**

In accordance with the Appraisal Independence Requirements, when there is a reasonable basis to believe an appraiser or Appraisal Management Company is violating applicable laws, or is otherwise engaging in unethical conduct, the matter must be promptly referred to the applicable State appraiser certifying and licensing agency or other relevant regulatory bodies.

- **Fannie Mae**

Any Seller that has a reasonable basis to believe an appraiser or Appraisal Management Company is violating applicable laws, or is otherwise engaging in unethical conduct, shall promptly refer the matter to the applicable State appraiser certifying and licensing agency or other relevant regulatory bodies.

FHA/HUD:

Allowing the removal of an appraiser from a list of qualified appraisers or the addition of an appraiser to an exclusionary list of qualified appraisers, used by any entity, without prompt written notice to such appraiser, which notice shall include written evidence of the appraiser's illegal conduct, a violation of the Uniform Standards of Professional Appraisal Practice (USPAP) or State licensing standards, improper or unprofessional behavior or other substantive reason for removal.

Audits of Fee Panels

The OCC bulletin of October 30, 2013 on Third Party Oversight, has placed greater emphasis upon a review of AMC (a third party) practices, policies and procedures. The focus of this paper is fee panel management. The lender, as well as their third parties, are responsible for appraiser selection. A lender can develop their own panel or they can delegate that task to their AMCs.

If they choose the latter, they should reasonably be auditing their Third Parties' fee panels. Those lenders who chose to use Appraisal Management Companies will need to closely monitor their fee panel policies, practices and procedures. Third Party Oversight will be covered in a separate white paper.

Property Data Collectors

With the introduction of alternative education from the Government Sponsored Enterprises, the CRN recommends the following standards:

1. Property Inspections - 7 hours
   Measuring by ANSI standards - 7 hours
   Professional Conduct – 3 hours

The CRN will be developing courses for Property Data Collectors.

2. Annual Criminal Background checks to include the following (which is the same standard proposed for appraisers):
   a. Arrest records
   b. National Criminal Search
   c. Terrorist Watch List
   d. Office of Foreign Asset Control (OFAC)
   e. Social Security Trace
   f. Federal District Criminal Search
   g. Sex Offender Registry

3. Competency Exam

Engaging an unlicensed, unregulated cohort introduces a different set of challenges. Due to a lack of licensing for this new cohort a lender, or their agent, you will need to consider how to monitor these activities. Areas of concern:

1. If a customer complains about the behavior of the Property Data Collector who will be responsible?
2. If the PDC makes a substantive error what will be your processes?
3. If a real estate agent is engaged and has a conflict of interest by inspecting a property for another in-house agent within the same brokerage, how will you prevent this situation?

Collateral Risk Network, Inc.

Summary

The benefit of adopting a best practices approach for fee panel management is that compliance will actually yield a reward of savings, promote mutually beneficial relationships with appraisers, keep your bank examiners happy, and assist with risk avoidance.

Frequently Asked Questions

Q. Can a lender provide a list to an AMC?
A. Yes, but the AMC should be assured through their Service Level Agreements (SLAs) that the lender's processes were compliant with Appraisal Independence Requirements.

Q. Can a loan officer nominate or suggest an appraiser to a panel provided the appraiser is properly vetted?
A. No. This is perhaps the most misunderstood component of AIR. The reason this is a prohibited practice is that the opportunity for abuse exists if someone in loan production nominates their "favorite" appraiser to a panel. Then in a blind rotation if there is only one appraiser on the panel in that market area, they are assured that their appraisal orders are directed to their appraiser of choice, ergo losing all independence as intended by Dodd Frank.

From Fannie Mae AIR FAQs: *Mortgage brokers and real estate agents must <u>not be involved in the selection of appraisers for an approved panel</u> or specific assignments under any circumstances. Please refer to Section IV.A for further information regarding who is authorized to select and retain appraisers.*

From Fannie Mae AIR FAQ:
Certain parties are prohibited from:
(a) Selecting, retaining, recommending, or influencing the selection of any appraiser for a specific assignment <u>or for inclusion on a list or panel</u> of appraisers approved or forbidden to perform appraisals for the Seller; and

Q. Is a check of the ASC Registry sufficient due diligence?
A. No for a number of reasons. First, 60% of the disciplinary actions do not appear in the ASC Registry. Second, evidence of a license does not denote either competence or ethics. I am sure many know someone with a driver's license who is an incompetent driver. The point being that an appraisal license or certification means that they have met the minimum criteria to obtain a credential.

Q.Is a round robin process a best practice?
A. Not really. The best appraiser for each assignment should be selected.

Q. Can a lender abdicate their risk and responsibilities of appraiser selection to a third party AMC?
A. No. Interagency Guidelines
that risk increases once a third party is engaged. The lender remains ultimately responsible.

Q. Is there anything to prohibit a mortgage broker from owning an AMC?
A. Not at the present time. (Note: at the time of this publication the AMC Final Rules have not been released.)

Q. Should a lender engage an AMC that is broker owned?
A. No. A broker who owns an AMC would be violating Appraisal Independence. There is an obvious conflict of interest. This would be revealed during a thorough due diligence process.

Q. Is the use of broadcast systems compliant?
A. It could be but generally not very likely. The best appraiser should be selected for each assignment.

Q. How do I establish a customary and reasonable fee?
A. An analysis of academic studies, independent private sector fee surveys, and the VA fee schedule.

Q. Is it a violation of USPAP for an appraiser to submit sample appraisal reports?
A. No. They can seek permission from the client or they can redact private information.

Q. Can background checks be shared?
A. Yes. A client should only accept a background check through a secure system.

Q. Should a background check company issue a pass/fail on an appraiser?
A. No. According to the OCC it would not be compliant for a third party to make that decision. The danger is that the third party would be creating a national "Do Not Use" list.

Q. Why do some clients require a letter of good standing from the State appraisal agency?
A. They would be fairly useless. Appraisers can have disciplinary actions that are serious but still maintain an active status.

Q. Can I pay my support staff a bonus based upon how cheaply they can engage the appraiser?
A. No. That would not be compliant. The lender or AMC are to engage the best appraiser, not the fastest and not the cheapest.

Q. If an appraiser accepts a fee then it must be C&R, correct?
A. No, it may be neither. Acceptance of a fee by an appraiser in no way is assurance that the fee is compliant with Dodd Frank.

Q. If that State ran a background check on the appraiser why should I run one?
A. At present most States do not run one and those that do generally do so only initially. There are a few exceptions. Again, it is not the State's role to perform your due diligence. Your standards would more than likely differ from the State's. There are quite a few appraisers with a criminal background who maintain valid credentials.

Summary of Guidance & Regulations

The relevant references in the guidance and regulations regarding fee panel management have been assembled as follows:

FIRREA, of 1989 vintage, maintains that the appraiser selected must be independent of loan production.

Appraiser Independence

Staff appraisers. *If an appraisal is prepared by a staff appraiser, that appraiser must be independent of the lending, investment, and collection functions and not involved, except as an appraiser, in the federally related transaction, and have no direct or indirect interest, financial or otherwise, in the property. If the only qualified persons available to perform an appraisal are involved in the lending, investment, or collection functions of the regulated institution, the regulated institution shall take appropriate steps to ensure that the appraisers exercise independent judgment. Such steps include, but are not limited to, prohibiting an individual from performing an appraisal in connection with federally related transactions in which the appraiser is otherwise involved and prohibiting directors and officers from participating in any vote or approval involving assets on which they performed an appraisal.(b) Fee appraisers. (1) If an appraisal is prepared by a fee appraiser, the appraiser shall be engaged directly by the regulated institution or its agent, and have no direct or indirect interest, financial or otherwise, in the property or the transaction.*

Fannie Mae Selection Criteria-- April 15, 2014

The lender is responsible for the selection of appraisers and for the <u>qualifications and quality of work provided by the appraisers that are selected</u>; may not use appraisals ordered or received by borrowers or other parties with an interest in the transaction, such as the property seller or real estate broker. Fannie Mae does allow lenders to use third--party vendors (for example, appraisal management companies) to manage the appraiser selection process. However, it should be noted that if a lender enters into a contract with any vendor, contractor, or third--party service provider, <u>the lender is accountable for the quality of the work performed as if it was performed by an employee of the lender.</u>

The lender (or its authorized agent) must establish policies and procedures to ensure that qualified individuals are being selected in accordance with Fannie Mae requirements, including the <u>Appraiser Independence Requirements.</u>The lender must ensure that an appraiser has demonstrated the ability to perform <u>high quality</u> appraisals before using an appraiser's services. The quality of an appraiser's work is a key criterion that must be used in determining which appraiser the lender (or its authorized agent) uses for its assignments. <u>The requirement for an appraiser to produce a high quality work product must always outweigh fee or turnaround time considerations.</u>

Delegating these responsibilities to a third party does not relieve the lender of its responsibilities related to the appraisal or the value, condition, and marketability of the property. See B4--1.3--12, Quality Assurance, for information related to ongoing review of appraisals.

Fannie Mae on Appraiser Selection

Fannie Mae requires a lender to use an appraiser who has the knowledge and experience that is required to perform a professional quality appraisal in a specific geographic location for the particular property type for which the lender needs an appraisal. The appraiser must also have knowledge about, and access to, the necessary and appropriate data sources for the area in which the appraisal assignment is located.

Freddie Mac on Appraiser Selection

FHLMC states Loan officers are prohibited from " Selecting, retaining, recommending, or influencing the selection of any appraiser for a particular appraisal assignment or for inclusion on a list or panel of appraisers approved or forbidden to perform appraisals for the Seller.

Excerpts from Interagency Appraisal and Evaluation Guidelines (December 2010)

Examiners will review steps taken by an institution to ensure that the persons who perform appraisals and evaluations are qualified, competent, and are not subject to conflicts of interest.

- *Provide for independence of the persons ordering, performing and reviewing appraisals.*
- *Establish selection criteria and procedures to evaluate and monitor the ongoing performance of appraisers.*
- *Implement internal controls that promote compliance with program standards and include monitoring of third-party arrangement.*

Selection of Appraisers

From Interagency Appraisal & Evaluation Guidelines:

An institution's collateral valuation program should establish criteria to select, evaluate, and monitor the performance of appraisers. The criteria should ensure that:

- *The person selected possesses the requisite education, expertise, and experience to competently complete the assignment.*
- *The work is periodically reviewed.*
- *The appraiser selected is capable of rendering an unbiased opinion*
- *The appraiser is independent.*
- *The appraiser holds the appropriate State certification or license at the time of assignment.*

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- *The work is periodically reviewed.*
- *The appraiser selected is capable of rendering an unbiased opinion*
- *The appraiser is independent.*
- *The appraiser holds the appropriate State certification or license at the time of assignment.*

The person who selects or oversees the selection must be independent of the loan production area.

Approved Appraiser List

If an institution establishes an approved appraiser list for selecting an appraiser, they should have appropriate procedures for the development of the list. These procedures should include a process for qualifying an appraiser for initial placement on the list as well as periodic monitoring of the appraiser's performance and credentials. It is a two-step process.

Engagement Letters

An institution should not allow the lower cost or the speed of delivery time to inappropriately influence the ordering decision.

An institution is accountable for ensuring that any services performed by a third party, both affiliated and unaffiliated, comply with applicable laws. An institution should have the resources and expertise necessary for performing ongoing oversight of third party arrangements.

An institution also is responsible for ensuring that a THIRD PARTY (also known as an Appraisal Management Company) selects an appraiser who is competent and independent, has the requisite experience and training for the assignment and thorough knowledge of the subject property's market. Appraisers must be appropriately certified or licensed but this minimum credentialing requirement is not sufficient to determine that an appraiser is competent to perform an assignment for a particular property or geographic area.

Loan production is prohibited from:

Selecting, retaining, recommending, or influencing the selection of any appraiser for a particular appraisal assignment or for inclusion on a list or panel of appraisers approved or forbidden to perform appraisals for the Seller.

Key components of Dodd Frank Title XIV:

- Mandatory Reporting
- Portability
- Customary & Reasonable Fees
- Appraiser Independence
- Copies to Borrower
- Additional powers to ASC
- AMC registration and oversight
- AVMs

AMC Minimum Requirements*:

- Register and be subject to supervision
- Verify the credentials
- AMCs must comply with USPAP

If a lender chooses to engage an AMC they cannot abdicate the responsibilities of compliance such as appraiser selection to a third party.

Note: The use of a third party increases risk, not decreases it, by definition. Unfortunately, it is a commonly held belief that one can outsource risk. An institution can mitigate risks and insure against certain risks but compliance is the responsibility of the financial institution. This is why oversight is so vitally important.

Darrin Benhart, Deputy Comptroller for Supervision Risk Management of the Comptroller of the Currency, in a presentation to the Mortgage Bankers Association on September 11, 2013, made the following statement:

- *We sometimes found little oversight of appraisal management companies (AMCs). In some cases, bankers didn't understand how appraisers were selected and engaged on behalf of the bank. This is a critical function where effective oversight was missing especially when the function was outsourced.*

It is worth noting the date this was delivered. This was just prior to the OCC's Third Party Oversight Bulletin, which was announced on October 31, 2013. In short, lenders are wholly responsible for the appraiser selection process even when they engage a third party.