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Rules Docket Clerk
Office of the General Counsel
Department of Housing and Urban Development
Room 10276
451 Seventh Street, SW
Washington, DC 20410-0500

RE: Docket No. FR-4722-P-01; Department of Housing and Urban Development; FHA Single Family Mortgage Insurance; Lender Accountability for Appraisals; 24 CFR Parts 25 and 203; 68 Federal Register 1765, January 13, 2003.

Dear Sir or Madam:

The American Bankers Association (“ABA”) appreciates the opportunity to comment on the Department of Housing and Urban Development’s (“HUD”) proposed rule imposing on FHA approved lenders strict accountability for the quality of appraisals on properties secured by Federal Housing Administration (“FHA”) insured mortgages. This letter supplements the joint letter to HUD on this proposed rule from the ABA, America’s Community Bankers, the American Financial Services Association, the Consumer Bankers Association, the Consumer Mortgage Coalition, and the Mortgage Bankers Association of America dated March 14, 2003.

The American Bankers Association brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership - - which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks - - makes ABA the largest banking trade association in the country.

Background

In order to further ensure the “accuracy and completeness of appraisals on projects securing FHA insured mortgages”, HUD proposes that lenders participating in the FHA single-family mortgage insurance program (“FHA Program”) be held “strictly accountable for the quality of appraisals” on FHA Program properties. Under the proposal, lenders that fail to ensure the quality of the appraisals required under the FHA Program will be subject to sanctions

imposed by the HUD Mortgagee Review Board. HUD intends that the proposed rule apply to “sponsor lenders, who underwrite loans, and loan correspondent lenders, who originate loans on behalf of their sponsors.”

ABA Position:

ABA recognizes HUD’s concern for protecting the integrity of the FHA Program and the important role quality appraisals play in achieving this objective. At the same time, ABA strongly objects to the imposition of a regulatory requirement that the lender have equal accountability with the appraiser for the performance of the appraisal and the content of the appraisal report. Such an approach ignores the independence of appraisers in the appraisal process and places lenders in the untenable position of having responsibility for activities for which they have no professional knowledge, training, or licensure.

HUD should not impose on lenders the same responsibility appraisers have for appraisals. To do so defies common sense just as much as if appraisers were held equally responsible with lenders for the lenders’ underwriting decisions.

The ABA believes that it is a bad public policy to create by regulation a requirement that lenders possess all of the knowledge, training, and licensure so as to place them in the role of the appraiser. To do so would impose such a level of liability and risk for lenders and their employees that in order to avoid this newly imposed liability they might refrain from participating in future FHA programs.

Instead of creating this regulatory roadblock to participation, HUD should address the issue of lender responsibility within the context of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (“FIRREA”). FIRREA establishes detailed criteria for the appraisal process as it involves federally related transactions. FIRREA creates a framework in which the states create licensing and certification mechanisms to ensure that real estate appraisers who meet the education and experience qualification criteria and successfully pass the state examination have a minimal level of professional competence.

In implementing FIRREA, the Federal financial institution regulatory agencies (“agencies”) have promulgated regulations and guidelines specifying the responsibilities of financial institutions within the context of the real estate appraisal process. This authority does not include any requirement that financial institutions be held strictly accountable for the work of appraisers.

By proposing this regulation, HUD blurs the distinction between lenders and appraisers and creates a regulatory accountability that has no basis in law and no equivalent among the Federal regulations governing financial institutions and their responsibilities in the appraisal process.

By way of example, in October 1994, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Reserve Board,

and the Office of Thrift Supervision, jointly issued their Interagency Appraisal and Evaluation Guidelines (“Guidelines”). The Guidelines expand on the regulations established by each of the agencies in response to FIRREA. The Guidelines hold the financial institutions regulated by these agencies accountable for their role as mortgage lenders and establish specific policies that relate to the independence of the appraisal function, the minimum appraisal standards that must be adhered to in conducting appraisals, the qualifications of individuals who perform appraisals, and the requirements relating to program compliance and portfolio monitoring.

Nowhere in the Guidelines do the agencies impose the level of accountability suggested by HUD in this proposed regulation. Instead, the Guidelines appropriately establish the responsibilities of financial institutions in their relationship with appraisers and the appraisal process. These responsibilities include establishing an appraisal and evaluation program to 1) “establish selection criteria and procedures to evaluate and monitor the ongoing performance of individuals who perform appraisals or evaluations”, 2) “provide for the independence of the person performing appraisals or evaluations”, and 3) “establish internal controls that promote compliance with these program standards” among other responsibilities. A financial institution’s responsibility does not extend to include strict accountability for the performance of the appraiser and for the quality of the appraisal report.

Financial institutions establish criteria for the “selection, evaluation, and monitoring of the performance of the individual(s) who perform a real estate appraisal or evaluation.” Under the Guidelines, these criteria ensure that the appraiser selection process is “non-preferential and unbiased”, that “the individual selected possesses the requisite education, expertise, and competence to complete the assignment”, that “the individual selected is capable of rendering an unbiased opinion”, and that “the individual selected is independent and has no direct or indirect interest, financial or otherwise in the property or the transaction.” Again, financial institutions have the responsibility to establish criteria for independence, competency, education, and expertise, but there is no requirement that financial institutions and their employees must possess this education, experience, and competency so as to be strictly accountable for the appraisal.

Thus, while financial institutions are responsible for initiating appraisals, ensuring their compliance with the agencies’ regulations and the Guidelines and overseeing the process through administrative review, they are not appraisers. They know the “red flags” to look for when working with appraisers and reviewing appraisal reports, but they are not trained as appraisers and do not perform that function.

In addition, the agencies in their regulations implementing FIRREA reference the Uniform Standards of Professional Appraisal Practice (“USPAP”), which, with limited modification, is applicable in every federally related transaction involving financial institutions. USPAP does not require strict accountability by lenders in the appraisal process.

In terms of its practical impact, HUD's finalization of this proposed regulation will impose significant burdens on financial institutions. As an example, financial institutions which operate in several states with a centralized underwriting function may be forced to unnecessarily review each property onsite so as to ensure that they meet the strict accountability standard imposed by HUD. Financial institutions may have to reduce their potential risk through the option of hiring their own staff of appraisers to perform appraisals instead of employing independent appraisers to perform this function. This could significantly add to the appraisal overhead costs. Also, HUD's imposition of this strict accountability standard could also result in enhanced litigation risks for financial institutions whereby plaintiffs filing lawsuits against appraisers could sweep financial institutions into the lawsuits under the strict accountability standard advocated by HUD. A better approach would be for HUD to require that appraisers have current and in force errors and omissions insurance in reasonable limits, proof of which should be certified to lenders and agencies upon request.

Conclusion:

The ABA urges HUD not to finalize this proposed regulation. Imposing a strict accountability standard on lenders is bad public policy. It will discourage lenders from participating in the FHA Program. It is contrary to FIRREA, the agencies' regulations and Guidelines, and USPAP. It will increase burdens, risk, and liability on financial institutions. Thus, HUD should seek alternatives to enhancing the integrity of the FHA appraisal process.

If you have any questions about this letter, please do not hesitate to contact the undersigned at 202-663-5333.

Sincerely,



John C. Rasmus