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<u>DELIVERED ELECTRONICALLY</u>

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW
Suite 3E–218
Washington, DC 20219

Ann E. Misback, Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Re: DEPARTMENT OF THE TREASURY Docket No. OCC–2018–0038
FEDERAL RESERVE SYSTEM Docket No. R–1639
FDIC RIN 3064–AE87—Real Estate Appraisals

COMMENTS OF APPRAISER ORGANIZATIONS

Dear Sir/Madam:

Constantine Cannon LLP, on behalf of the thirty listed state appraiser organizations[1] (the "Appraiser Organizations"), respectfully submits these Comments in opposition to the Notice of

[1] Appraiser's Coalition of Washington
Association of Georgia Real Estate Appraisers
Arizona Association of Real Estate Appraisers
Arkansas Appraisers Association
California Coalition of Appraisal Professionals
Coalition of Appraisers in Nevada
Delaware Association of Appraisers
Georgia Coalition of Appraisal Professionals
Idaho Coalition of Appraisal Professionals
Illinois Coalition of Appraisal Professionals
Kentucky Association of Real Estate Appraisers
Louisiana Real Estate Appraiser Coalition
Maryland Association of Appraisers
Michigan Coalition of Appraisal Professionals
Mississippi Coalition of Appraisers
New York Coalition of Appraiser Professionals
North Carolina Real Estate Appraiser Association
North Dakota Appraisers Association
Northern Colorado Association of Real Estate Appraisers
Ohio Coalition of Appraisal Professionals
Oklahoma Professional Appraisers' Coalition
Professional Appraisers Association of South Dakota
Real Estate Appraisers Association (CA)
Real Estate Appraisers of Southern Arizona
Rhode Island Real Estate Appraiser Association
South Carolina Professional Appraisers Coalition
Tennessee Appraiser Coalition
United Appraisers of Utah
Virginia Coalition of Appraiser Professionals
West Virginia Council of Appraiser Professionals

Proposed Rulemaking ("NPRM" or "proposed rule") by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation ("the agencies") to raise the *de minimis* exemption for appraisals for federally-related residential real estate transactions from $250,000 to $400,000. Additional outreach from the agencies on the proposed rule is necessary, and the Appraisers Organizations respectfully request the agencies conduct a hearing to receive input from the various stakeholders on the impact of the proposed rule.

INTRODUCTION

The Appraiser Organizations believe that the issues raised by the NPRM have broader implications for consumers and residential mortgage sector participants beyond the relatively small number of federally-related transactions to which the exemption directly applies. Rather, the outcome of the NPRM will signal to lenders and purchasers of residential mortgages the relative importance of appraisals versus evaluations in the mortgage process, leading those participants to increase their own *de minimis* exemptions or to increase the use of appraisal waivers.

While the NPRM asks a series of questions regarding the proposal to raise the existing exemption by $150,000, the NPRM's justification for the increase is flawed in two significant ways. **First, the agencies ignore the statutorily-protected interests of home buyers by assessing the merits of the increase primarily in terms of the NPRM's potential impact on financial institution safety and soundness, essentially as an exercise in portfolio risk management for individual institutions and for the mortgage sector**. From this perspective, the exemption is merely an inflation adjustment that likely would have limited impact on portfolio risk.

This approach ignores the consumer-focused provisions added to the residential mortgage origination process by the Dodd-Frank Wall Street Reform and Consumer Protection Act's ("Dodd-Frank Act" or "Dodd-Frank") amendments to the Truth-in-Lending Act ("TILA") and related amendments to the Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA"). These provisions are designed to protect the soundness of *individual* mortgage transactions and thus to reduce the potential injury to *individual* homebuyers from having a mortgage based on an above-market or otherwise inappropriate appraisal.

This concern for harm to individual borrowers is the antithesis of the portfolio risk management approach that permeates the NPRM. In the Dodd-Frank regulatory environment, the agencies' analysis must assess the number and characteristics of the potential homebuyers who will be excluded from the protection of an appraisal, e.g., low-income and first-time buyers. But the agencies' contrary focus on portfolio-risk management is made clear in the NPRM's statistical assessment which shows that, although the number of exempt federally-related

mortgage transactions would grow by 18 percentage points to 72 percent of such transactions, only 35 percent of the cumulative dollar amount of such transactions would be exempted. Because this number was less than the dollar-amount volume exempted in 1994, the agencies conclude in the NPRM that the $400,000 exemption would "be less likely to impose a safety and soundness risk" than was the case in 1994.

Second, and just as importantly, the agencies assume that an "evaluation" of a home's value, under open-ended and nearly non-existent standards, could somehow be a meaningful substitute for an appraisal statutorily required to be compliant with the Uniform Standards of Professional Appraisal Practice ("USPAP"). Recent industry announcements foreshadow "black box" solutions that combine automated valuation models ("AVM") (for which the agencies have yet to promulgate statutorily required standards) with photos provided by drones or other sources. As the volume of data from actual appraisals declines, AVM-based evaluations will necessarily "drift" from reality, particularly in areas where almost all, if not all, residential transactions fall within an appraisal exemption. Although the agencies released "guidelines" for such evaluations in 2010, no rules governing evaluations are in place—and none that reflect the mortgage industry's increasing reliance on technology to substitute for informed professional judgment.

The sole alleged benefit to consumers from such harms is that evaluations should cost less than appraisals and have a shorter "turn time." Again, such claims are more illusory than real. While the NPRM cites no data on the cost to consumers of evaluations, the Appraiser Organizations believe that the potential cost of such evaluations might be only zero to 20 percent less than the cost of an appraisal on a similar property —a truly trivial cost compared to the financial harm from purchasing a home with a price and mortgage justified by an erroneously high valuation, rather than an appraisal based on information provided by a trained appraiser with knowledge of the local market. National application of a $400,000 exemption will also have disparate impacts among various U.S. regions—with almost all mortgage transactions excluded in some regions or metropolitan statistical areas. Moreover, in the experience of Appraiser Organizations' members, the standard 5-day turn time is not likely to impinge on the closing of a mortgage transaction.

In sum, the Appraiser Organizations believe that the justifications put forward by the agencies will leave increasing numbers of consumers vulnerable to the vagaries of a valuation process that is not supported by a regulated professional assessment. The agencies appear prepared to put individual homebuyers at risk—particularly low income and first-time buyers—in the name of promoting "efficient" mortgage processing, apparently designed merely to satisfy the portfolio risk management algorithms of banks and portfolio purchasers. The NPRM even argues that the track record under the current $250,000 exemption demonstrates that defaults increased only dramatically during the financial crises and the years immediately thereafter, implying that the Dodd-Frank objective to avoid harm to individual homeowners and the

mortgage sector would be met so long as defaults under a $400,000 exemption did not reach crisis levels—except during the next financial crisis or recession.

In the sections that follow, these Comments will set out in more detail the reasons why the agencies should keep the exemption at $250,000. In so doing, they will identify the relevant NPRM Questions addressed, and propose a potential alternative—basing the level of the *de minimis* exemption on regional housing prices instead of a national, flat rate.

DISCUSSION

I. The NPRM Fails to Recognize the Dodd-Frank Act's Emphasis on Appraisals and Supervision of Appraisal Quality as a Consumer Protection Measure for Homeowners.

A. Dodd-Frank Prevents the Agencies from Treating the Appraisal Requirement Merely as a Tool for Portfolio Risk Management.

A key flaw in the NPRM's proposal is that it presumes that the appraisal requirement's primary purpose continues to be as a mortgage portfolio risk-management tool for insured financial institutions. While such an approach might have been plausible prior to the passage of the Dodd-Frank Act, it is untenable under the statutory mandates that exist today.

In response to the 1980's savings and loan crisis, Congress passed FIRREA, whose first purpose was "[t]o promote, through regulatory reform, a safe and stable system of affordable housing finance."[2] Because use of appraisals conducted by licensed/certified appraisers in federally-related residential and commercial real estate transactions was a central method of achieving this objective, FIRREA Title XI established the framework governing such appraisals, including establishment of the Appraisal Subcommittee and specifying the role of state appraisal licensing agencies.

As set out in the NPRM, FIRREA sections 1111-13 authorized the federal financial regulatory agencies to determine which categories of federally-related transactions require state certified appraisers; the remainder required appraisals by "licensed" appraisers. The Federal Reserve was the first agency to establish a *de minimis* exemption. In a 1990 NPRM, it proposed setting the exemption under 12 C.F.R. § 225.63(a)(1) at $15,000.[3] When finally adopted, however, this amount was increased to $100,000, because the Board found no "evidence that transactions below $100,000 have posed systemic risks as well as the protections afforded to

[2] Pub. L. No. § 101-73 § 101(1), 12 U.S.C. § 1811 note.
[3] 55 Fed. Reg. 4,810-11 (Feb. 9, 1990).

individual regulated institutions by the inter-agency appraisal guidelines."[4] Other financial agencies adopted the Board's proposal.

When the agencies again considered the issue in 1994—proposing to raise the exemption to $250,000—they again focused on risk to financial institutions and the financial system, with consumer protection relegated to a secondary concern:

> Many appraisers also stated that appraisals by certified or licensed appraisers are necessary to protect the consumer. The agencies believe that this assertion mischaracterizes the role of the institution's determination of collateral value in a typical consumer transaction. The regulated institution obtains the appraisal or evaluation as part of its loan underwriting process in order to make certain that it is adequately secured. Any appraisal ordered by a financial institution is not designed, and generally comes too late, to assist the consumer in negotiating a contract price. In a purchase of real estate, the purchase offer is generally made before financing is sought and the financial institution orders an appraisal. Therefore, the appraisal represents an after-the-fact cost. Further, even when a Title XI appraisal is not required, nothing prevents a consumer from independently obtaining an appraisal by a licensed or certified appraiser for the consumer's own use in the negotiating process. Moreover, the agencies' rules require an institution to obtain an appropriate evaluation of the real property collateral for transactions below the threshold, and that evaluation would be available to the consumer.
>
> *The agencies believe that many of the concerns about consumer protection are addressed under statutory and regulatory programs other than Title XI of FIRREA, which focuses on bank and thrift safety and soundness.*[5]

Remarkably, "85 percent of the dollar volume of mortgages financing new homes and 82 percent of the volume of mortgages financing purchases of existing homes will fall below the $250,000 threshold."[6] Just as remarkably, "[t]he increase in 1-to-4 family residential real estate loans exempted by the $250,000 threshold will not affect safety and soundness, as these loans are traditionally the safest in a lending institution's portfolio."[7] Of course, that assessment was true—until it wasn't.

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[4] 55 Fed. Reg. 27,762, 27,764 (July 5, 1990).
[5] 59 Fed. Reg. 29,482, 29,485 (June 7, 1994) (emphasis added).
[6] *Id.* at 29,486.
[7] *Id.*

B. Dodd-Frank's Amendments to TILA Impose an Obligation on the Agencies to Give Equal Weight to the Impact on Individual Homebuyers of Increasing the Exemption.

The 2007-08 mortgage crisis led to enactment of Title XIV of the Dodd-Frank Act, incorporating provisions of the house-passed Mortgage Reform and Anti-Predatory Lending Act.[8] These reforms went beyond FIRREA Title XI appraisal requirements, with their federally-related transactions focus, by adding consumer-focused appraisal requirements to the TILA.

New TILA section 129E[9] established multiple "Appraisal independence requirements" for consumer credit transactions secured "by the principle dwelling of the consumer," regardless of whether they were also federally-related transactions. These provisions protect individual consumers from obtaining mortgages supported by appraisals that have been affected by any of numerous forms of misconduct that could compromise an appraiser's independence. Dodd-Frank also added TILA section 129H,[10] which established additional consumer protection requirements for certain "high-risk" mortgages (those with higher than average prime offer interest rates), regardless of whether they are also federally-related transactions. These include the requirement for an appraisal conducted by a credentialed appraiser pursuant to USPAP "who conducts a physical property visit of the interior of the mortgaged property," as well as a second appraisal for a property that is being resold within 180 days of a prior purchase.[11]

The federal financial agencies' "safe harbor" requirements for the required on-site appraisals include lender confirmation that the appraisal, for example, addresses conditions in the property's neighborhood, addresses the condition of the property and any improvements to the property, indicates which valuation approaches were used, includes a reconciliation if more than one valuation approach was used, and indicates that a physical property visit of the interior of the property was performed.[12] The *de minimis* exemption for such appraisals currently is $26,000.[13] This low level demonstrates that consumers being charged above-standard interest rates, who are likely to be in adverse credit circumstances, were to be given protection, even though a default on a secured loan of such a small amount is unlikely to place a financial institution at prudential

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[8] H.R. 1728, 111th Cong. (2009).
[9] 15 U.S.C. § 1639e.
[10] 15 U.S.C. § 1639h.
[11] 15 U.S.C. §§ 1639h(b)(1), (2)(A).
[12] *See* 12 C.F.R. pt. 226, App. N.
[13] 12 C.F.R. § 226.43(b)(2), official staff interpretation 43(b)(2)[3]b.

risk. Finally, Dodd-Frank added FIRREA section 1126[14] that prohibits "broker price opinions"[15] from being used as the primary basis for valuing property used to secure a residential mortgage.

The federal financial regulatory agencies themselves recognized this increased consumer protection objective under Dodd-Frank in their July 31, 2017 NPRM raising the *de minimis* exemption for commercial—but not residential—real estate transactions to $400,000:

> [A]ppraisals can provide protection to consumers by helping to assure the residential purchaser that the value of the property supports the purchase price and the mortgage amount. The consumer protection role of appraisals is reflected in amendments made to Title XI and the Truth in Lending Act (TILA) through the Dodd-Frank Act governing the scope of transactions requiring the services of a certified or licensed appraiser. These include the addition of the CFPB to the group of agencies assigned a role in the appraisal threshold-setting process for Title XI and a new TILA provision requiring appraisals for loans involving "higher-risk mortgages."[16]

The agencies also recognized the broader scope of these consumer protection objectives when they established rules for implementing appraisal management company ("AMC") minimum standards for state appraiser agencies under new FIRREA section 1124.[17] They noted that:

> The proposed definition did not limit the definition of "covered transaction" to Federally related transactions … even though Title XI of FIRREA and its implementing regulations have applied historically only to appraisals for Federally related transactions. … Applying coverage of the AMC rule beyond Federally related transactions is consistent with the structure and text of other parts of section 1124, most of which address appraisals generally rather than appraisals only for Federally related transactions. … In particular, the text of section 1124(a)(4) indicates that one of the chief purposes of the minimum requirements for AMCs is to ensure compliance with the valuation independence standards established pursuant to section 129E of TILA.[18]

In justifying their decision not to increase the exemption from $250,000, the agencies also addressed the impact of increasing the exemption threshold on risk:

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[14] 12 U.S.C. § 3355.

[15] Defined as "an estimate prepared by a real estate broker, agent, or sales person that details the probable selling price of a particular piece of real estate property and provides a varying level of detail about the property's condition, market, and neighborhood, and information on comparable sales, but does not include" an AVM. *Id.*

[16] 82 Fed. Reg. 35,478, 35,481 (July 31, 2017, footnotes omitted).

[17] 12 U.S.C. § 3353.

[18] 80 Fed. Reg, 32,657, 32,664 (June 9, 2015).

> [T]he agencies considered safety and soundness concerns that could result from a threshold increase for residential transactions. As the EGRPRA Report noted, the 2008 financial crisis showed that, like other asset classes, imprudent residential mortgage lending can pose significant risks to financial institutions.[19]

The NPRM, however, sought to downplay the role of improper appraisals, finding that, on the basis of "supervisory experience," the losses during the financial crisis were attributable to "a number of factors."[20] While undoubtedly true, such an assessment is at variance with the Final Report of the Financial Crisis Inquiry Commission, which the NPRM itself summarizes:

> In its final report, the National Commission on the Causes of the Financial and Economic Crisis in the United States documents the pressure appraisers were under from mortgage lenders, brokers, and others with an interest in generating loan volume, to meet target values in order to complete loan transactions.[21]

The agencies then note the reforms contained in Dodd-Frank and agency Guidelines have reduced the potential for the recurrence of the problematic conduct that the National Commission found.

The agencies similarly dismiss reality when they argue that the level of residential mortgage defaults remained largely constant after the 1994 increase to $250,000, *except for the five years beginning with the 2008 mortgage crisis*.

> [T]he net charge-off rate for residential real estate transactions increased significantly from 2008 through 2013, which was during and immediately after the recent recession, ranging from 63 basis points to 204 basis points. This data suggests that the loss experience associated with residential real estate loans generally stayed at a relatively consistent low rate except during the most recent crisis. … However, the loss rates declined to historical levels for all regulated institutions in 2014, indicating that the increase in the appraisal threshold in 1994 was not a significant contributing factor to the safety and soundness of regulated institutions, regardless of their size, during the recent recession.[22]

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[19] 83 Fed. Reg. 49,857-58 (Oct. 3, 2018).
[20] 83 Fed. Reg. at 63,110, 63,117 (Dec. 7, 2018).
[21] *Id.* at 63,117 & note 79.
[22] *Id.* at 63,118.

Thus, "[t]he agencies do not have data that show that raising the appraisal threshold would result in increased loss rates. … [T]he agencies' supervisory experience suggests that an increase in the threshold is unlikely to pose a safety and soundness risk to financial institutions."[23]

In presuming, for the purposes of this NPRM, that evaluations can serve as acceptable substitutes for appraisals, the agencies fail to consider that they have not yet fulfilled their responsibilities under Dodd-Frank-added FIRREA section 1125(b), 12 U.S.C. 3354(b), which directs the financial regulatory agencies to adopt regulations implementing specified standards for "automated valuation models used to estimate collateral value for mortgage lending purposes" for mortgages "secured by a consumer's principal dwelling." Such "Automated valuation models shall adhere to quality control standards designed to-

> (1) ensure a high level of confidence in the estimates produced by automated valuation models;
> (2) protect against the manipulation of data;
> (3) seek to avoid conflicts of interest;
> (4) require random sample testing and reviews; and
> (5) account for any other such factor that the agencies listed in subsection (b) determine to be appropriate."[24]

If adopted, enforcement power would be granted to the financial regulatory agencies, the Federal Trade Commission, the Consumer Financial Protection Bureau, and state attorneys general.

While the federal financial agencies' 2010 Interagency Appraisal and Evaluation Guidelines set out considerations to be used in including AVM results as part of any evaluation,[25] the Appraiser Organizations believe that the increasing use of "big data" risk management and valuation tools by government-sponsored enterprises ("GSEs") and third-party providers has increased lenders' willingness to base evaluations on such AVMs and associated applications beyond the use that may have been anticipated at the time the Guidelines were issued. In particular, the AVM is a "black box" approach in which the "reasoning" and weighting undertaken by the tool's algorithms may neither be fully understood by lenders nor comprehensible to prospective homeowners. Indeed, the NPRM concedes as much:

> [T]he agencies recognize that … appraisals provide more property information to a consumer than an evaluation. Given that evaluations are not required to be in a standard form and specific content is not mandated, it is also possible that some evaluations might be more difficult for consumers to understand or lack

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[23] *Id.*
[24] 12 U.S.C. § 3354(a).
[25] 75 Fed. Reg. 77,449, 77,468-69 (Dec.10, 2010).

information about the property typically included in an appraisal that could be useful to a consumer.[26]

Because affected homebuyers are likely to be low income or first-time buyers, this loss of consumer information is appropriately compared to the increased consumer appraisal protections offered for prospective homebuyers receiving high-priced mortgages pursuant to TILA 129H—for which the agencies' *de minimis* exemption is currently $26,000. Indeed, this low exemption threshold suggests that the current $250,000 FIRREA exemption level should be lowered, not raised.

II. Appraisals Offer Consumers Significant Information and Assurances Compared to Evaluations (Addressing Questions 3, 4, and 7).

Either by design or as a direct effect, the proposed rule will diminish the usage of residential real estate appraisals in favor of real estate evaluations. As a consequence, home buyers will be deprived of detailed information and qualified assurances from licensed and regulated professionals on the value of their property.

Unlike evaluations, residential appraisals are regulated by both the federal government and by all 50 states. Since the enactment of FIRREA in 1989, residential appraisers must conform to USPAP—the ethical and performance standards established and updated regularly by the Appraisal Foundation and its Appraisal Standards Board. USPAP was created "to promote and maintain a high level of public trust in appraisal practice by establishing requirements for appraisers."[27] In fact, the USPAP requirements contain ethical, record keeping, competency, and scope of work rules along with various "Standards" for different types of appraisals.[28] In addition to USPAP, FIRREA also ensured that the Appraiser Qualification Board ("AQB") would establish Real Property Appraiser Qualification Criteria.[29] The AQB's qualification criteria mandate state appraiser licensure and certification requirements. FIRREA empowers the states to regulate and enforce USPAP and AQB qualifications, but states are free to establish additional regulatory safeguards for the appraisal process.

In stark contrast to appraisals, an evaluation is an open-ended method of valuing residential property with limited federal guidance or regulation. Specifically:

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[26] 83 Fed. Reg. at 63,115.
[27] Appraisal Standards Board & The Appraisal Foundation, *Uniform Standards of Professional Appraisal Practice (USPAP)* 2018-2019 ed. at 1, https://appraiserelearning.com/wp-content/uploads/2018/09/2018-19-electronic-copy-of-USPAP.pdf.
[28] *Id.*
[29] Appraisers Qualification Board & The Appraisal Foundation, *The Real Property Appraiser Qualification Criteria and Interpretations of Criteria* (May 1, 2018), https://appraisalfoundation.sharefile.com/share/view/scbea7640298440aa.

- "An evaluation is not required to be completed by a state licensed or state-certified appraiser or to comply with USPAP."
- "Unlike an appraisal report that must be written in conformity with the requirements of USPAP, there is no standard format for documenting the information and analysis performed to reach a market value conclusion in an evaluation."
- "An individual who prepares an evaluation may consider one or more valuation approaches or methodologies to estimate the market value of real estate."[30]

The financial agencies have provided Statements of Policy concerning the development and content of acceptable evaluations.[31] While the agencies do offer some criteria, e.g. "identifying the location of the property," the agencies allow the evaluator a significant degree of deference including allowing evaluations to be created by "an analytical method or a technological tool" instead of being prepared by a competent and licensed individual.[32] Indeed, an evaluation can be completed by a "bank employee or by a third party."[33] Given the lax requirement on who performs the evaluation, it is not inconceivable that a bank, or other interested party in the home's valuation, could distort the value through the evaluation process. In contrast, the regulatory oversight of the appraisal process ensures that such conflicts of interests are minimized.

In addition to the regulatory differences between the two valuation processes, there are also significant concerns about whether evaluations can effectively provide consumers with an accurate assessment on the value of a home. For example, the agencies have warned that a "sales comparison" evaluation will be ineffective "in areas where there have been few, if any, recent comparable sales of similar properties in reasonable proximity to the subject property."[34] Recently, the Federal Reserve Board commissioned a research study that found that AVM and owner valuations offered "similar information about the market value of homes," but the "degree of precision" was low—only half of AVM estimates were "within 10 percent of the sales price."[35]

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[30] Board of Governors of the Federal Reserve System, FDIC, Office of the Comptroller of the Currency, *Interagency Advisory on Use of Evaluations in Real Estate-Related Financial* Transactions (Mar. 4, 2016), https://www.occ.gov/news-issuances/bulletins/2016/bulletin-2016-8a.pdf.
[31] FDIC, *Interagency Appraisal and Evaluation Guidelines*, https://www.fdic.gov/regulations/laws/rules/5000-4800.html#fdic5000interagencyaae.
[32] *Id.*
[33] *Supra* note 30.
[34] *Id.*
[35] Raven Molloy & Eric Nielsen, *How Can We Measure the Value of a Home? Comparing Model-Based Estimates with Owner-Occupant Estimates*, Board of Governors of the Federal Reserve System – FED Notes (Oct. 11, 2018), https://www.federalreserve.gov/econres/notes/feds-notes/comparing-model-based-estimates-with-owner-occupant-estimates-20181011.htm.

As well as the federal government's own apprehensions over the inaccuracy of evaluations, the National Association of REALTORS ("NAR") has also noted its "concern[s] about the varying quality of valuation tools used by lenders for transactions that fall outside of the federal requirements for an appraisal."[36] In particular, NAR has stated that "[s]ome of the on-line automated valuation tools available today are not sophisticated enough to be relied on for an accurate valuation of real property" and usage of these evaluations could "severely under- or over-estimat[e]" a property's value.[37]

Moreover, there is no consumer recourse for a faulty evaluation. In the event a potential homeowner or lender receives an inaccurate appraisal, that individual or entity may file an official complaint with a state's appraiser board. Upon review of the complaint, the board may penalize the appraiser, and in some instances, revoke his or her license to appraise residential properties. In contrast, there is no independent review for faulty evaluations. Instead, consumers are left without remedy and cannot seek judgment from a state or federal agency. Therefore, by increasing usage of evaluations over appraisals, the proposed rule diminishes consumer protection over the home purchasing process, and in particular, limits consumer protection on many middle to low-income home purchasers in favor of appraisals for only high-value residential properties.

III. The Cost and Time for an Appraisal Does not Limit its Value to Consumers (Addressing Questions 1 and 2).

The total value of the appraisal—the certified valuation of a residential property performed by a licensed and regulated individual subject to federal standards and state law—is a significant benefit to home buyers. The Appraiser Organizations do not dispute the NPRM's statement that "evaluations… require less time to review than appraisals because they contain less detailed information," but that statement misses the point of protecting the single largest consumer purchase in the United States.[38] In reality, the added cost and time of doing an appraisal is, at most, modest when compared to the risks and costs a home buyer faces if the residential property is mis-valued. Specifically, as of 2018, the average cost of an appraisal was $331.00,[39] while the average turn time on a residential appraisal is around five days.[40] Given the

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[36] *Modernizing Appraisals: A Regulatory Review and the Future of the Industry, Hearing Before the H. Comm. on Financial Services,* 114th Cong. 2 (2016) (Statement of the National Association of REALTORS), https://narfocus.com/billdatabase/clientfiles/172/1/2787.pdf.

[37] *Id.*

[38] 83 Fed. Reg. at 63122.

[39] Brian O'Connell, *What is the Cost of Home Appraisal and What Should I Know?*, THE STREET (Aug. 17, 2018), https://www.thestreet.com/personal-finance/real-estate/home-appraisal-cost-14673950.

[40] For appraisals under the Veteran Affairs Home Loan program, appraisals, depending on the state, are required to be completed anywhere from five to ten business days. U.S. Dep't of Veteran Affairs, *VA Appraiser Fee Schedule*

benefits to the home purchaser, neither the cost nor the turn time of appraisals warrants a change to the *de minimis* exemption.

While the proposed comment suggests that there may be "material costs savings" in moving the residential real estate industry away from appraisals, the agencies' statement lacks evidentiary support. In addition to the limit of such potential cost savings, there is no guarantee such monies will be passed on to consumers. In fact, it is highly likely that only the lenders will realize any minimal cost savings. Moreover, the true cost to the consumer is not just the cost of the appraisal but also includes the fees associated with the lender utilizing third parties—AMCs—to manage the appraisal process. In their role as the intermediary between the lender and the appraiser, some AMCs charge consumers significant management fees for their retention of the appraiser to conduct the valuation of the home. In fact, these fees can nearly double the cost to the consumer, even while the appraisal fee remains unchanged.[41] An increase to the *de minimis* exemption will not address that ever-increasing cost to consumers.

Furthermore, the impact of such average costs and appraisal turnaround times are minimal compared to the cost to a consumer of obtaining a mortgage based on a mis-valued home. Even before the savings and loan crisis of the 1980s, improper home valuation was a leading cause of home foreclosures.[42] In fact, inaccurate valuations were a significant cause of the recent 2008 housing crisis,[43] which led to over eight million foreclosures between 2008 and 2010.[44] To quote the Federal Financial Institutions Examination Council's March 2017 Joint Report to Congress:

> The last financial crisis showed that, like other asset classes, imprudent residential mortgage lending can pose significant risks to financial institutions. In addition, the agencies recognize that appraisals can provide protection to consumers by

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and Timeliness Requirements, https://www.benefits.va.gov/HOMELOANS/appraiser_fee_schedule.asp (last visited Feb. 4, 2019).

[41] Kenneth R. Harney, *Are you paying unseen add-on fees for your appraisal?*, CHICAGO TRIBUNE (Mar. 21, 2017), https://www.chicagotribune.com/classified/realestate/ct-re-0326-kenneth-harney-20170322-column.html (Finding that AMCs can "add 35 to 50 percent surcharges — or more — onto the final bill to the consumer.").

[42] *See* Robert Bruss, *Bad Appraisals No. 1 Cause of Foreclosures*, CHICAGO TRIBUNE (Oct. 19, 1985) ("But if you ask home mortgage lenders about their foreclosures, most will tell you their No. 1 cause of losses is bad appraisals."), https://www.chicagotribune.com/news/ct-xpm-1985-10-19-8503130011-story.html.

[43] Joe Eaton, *The Appraisal Bubble*, THE CENTER FOR PUBLIC INTEGRITY (June 17, 2009) (updated May 19, 2014), https://publicintegrity.org/environment/despite-new-rules-appraisers-say-pressure-remains/ (noting that appraisers were pressured by lenders to inflate the value of the appraisal).

[44] ATTOM Staff, *U.S. Foreclosure Activity Drops to 12-Year Low in 2017*, ATTOM Data Solutions (Jan. 16, 2018), https://www.attomdata.com/news/foreclosure-trends/2017-year-end-u-s-foreclosure-market-report/.

> helping to assure the residential purchaser that the value of the property supports the mortgage amount assumed.[45]

Eliminating appraisals on homes valued between $250,000 and $400,000 will only increase the risk of more foreclosures. Moreover, while the costs and turnaround time on appraisals is a known quantity, there is little to no data on costs or turnaround time on evaluations. As a result, it is impossible to determine what consumers would pay or how long they would wait to receive an evaluation instead of an appraisal and if those supposed cost-savings would somehow outweigh the benefits of a regulated appraisal. In fact, the FDIC estimates that allowing small, covered institutions to switch from appraisals to evaluations will only save those institutions $321.75 per year, or less than .01 percent of such institution's non-interest expenses.[46] The foreclosure of a single home would eliminate such inconsequential savings to a lender; and foreclosure of any mis-valued home would potentially wipe out the life savings of the borrower.

Furthermore, while cost and turn time are important considerations, the government has long recognized that a valuation of residential property should comport with "safe and sound" procedures and the valuation method should not be used "solely because it provides the highest value, the lowest cost, or the fastest response or turnaround time."[47] It was less than two years ago that the agencies rejected the same proposal to increase the *de minimis* exemption from $250,000 to $400,000 noting that its decision again rested on "considerations of safety and soundness and consumer protection."[48] That decision did not take into account minimal savings on cost and time of appraisals and neither should this proposed rule.

If the agencies are concerned with the time and costs of appraisals, the answer should be to conduct outreach and gather information to create a proposed rule that could limit costs and time, not effectively eliminate appraisals for a significant portion of American consumers. The Appraiser Organizations would welcome the agencies working directly with lenders and appraisers to address any such concerns; however, this proposed rule does not appropriately address those issues.

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[45] Federal Financial Institutions Examination Council, Joint Report to Congress, Economic Growth and Regulatory paperwork Reduction Act at 35 (Mar. 2017), https://www.ffiec.gov/pdf/2017_FFIEC_EGRPRA_Joint-Report_to_Congress.pdf.
[46] 83 Fed. Reg. at 63,123.
[47] FDIC, Interagency Appraisal and Evaluation Guidelines, https://www.fdic.gov/regulations/laws/rules/5000-4800.html.
[48] *Supra* note 45.

IV. The Proposed Increase Would Have a Disproportionate Impact on Lower Income and First-Time Home Purchasers and Fails to Take Into Account Regional Differences in Home Prices (Addressing Questions 8 and 9).

The proposed rule states that raising the threshold amount from $250,000 to $400,000 is largely in response to comments received in other proceedings and in response to "a variety of house price and inflation indices."[49] But a flat 60 percent increase in the *de minimis* exemption in response to supposed housing price inflation ignores both consumer welfare and largely misses significant regional differences in housing prices.

By raising the exemption by $150,000, the proposed rule will ensure that low-income home purchasers will not be afforded the protections of an appraisal for their home purchase. Such an increase would largely impact first-time home buyers, the majority of whom are just starting in their careers and are of lesser means. In fact, the average household income for a first-time homeowner is $75,000, and the average cost of the first home is $190,000.[50] Therefore, the proposed rule favors higher-income and second-time home purchasers, directly counter to the very purpose of the laws that seek to protect vulnerable consumers.

In addition, the basis for the flat 60 percent increase lacks merit and fails to account for regional variation in home prices. According to the proposed rule, the increase in the *de minimis* exemption is not based on average home prices but instead "is consistent with general measures of inflation across the economy reflected in the [Consumer Price Index ("CPI")] since 1994, when the current appraisal threshold of $250,000 was set."[51] Inflationary changes are no basis for raising the *de minimis* exemption. First, given the available government data sources, CPI is not the best indicator of housing prices. In fact, CPI does not "take into account home sales prices" but instead "figures how much the owner of a house would have to pay each month to live there."[52] Second, according to United States Census data, as of October 2018, sales prices on homes throughout the United States were below the $400,000 threshold with a median price of $302,400.[53] In fact, according to NAR data, the median home price as of December 2018 is even lower than governmental data—$253,600.[54] These figures are significantly lower than the

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[49] 83 Fed. Reg. at 63,116.
[50] Kelsey Ramirez, *Here's what today's first-time homebuyers look like*, HOUSINGWIRE (Nov. 14, 2017), https://www.housingwire.com/articles/41813-heres-what-todays-first-time-homebuyer-looks-like.
[51] 83 Fed. Reg. at 63,117.
[52] Peter Coy, *The Consumer Price Index May Be Getting Inflation Wrong*, BLOOMBERG (May 2, 2018), https://www.bloomberg.com/news/articles/2018-05-02/the-consumer-price-index-may-be-getting-inflation-wrong.
[53] U.S. Census Bureau, HUD, *Monthly New Residential Sales, November* 2018, https://www.census.gov/construction/nrs/pdf/newressales.pdf (last visited Feb. 4, 2019).
[54] National Association of REALTORS, *National Existing Home Sales*, https://www.nar.realtor/sites/default/files/documents/ehs-12-2018-breakouts-of-single-family-condo-and-co-op-2019-01-22.pdf (last visited Feb. 4, 2019).

inflation indices relied upon by the proposed rule that presume median housing prices are over $600,000.[55]

More importantly, a blanket *de minimis* exemption fails to account for or acknowledge wide-ranging variations on housing prices across the United States, which reflect the truism that the key factors in housing prices are location, location, and location. According to the most-recent NAR data, of the United States' 146 metropolitan statistical areas ("MSAs"), only 17 MSAs have a median sales price for single-family homes that exceeds $400,000.[56] Under the proposed rule, nearly the entire housing stock for numerous cities and regions would fall below the proposed level. As an example, please see the attached Exhibit 1 (Charlotte, North Carolina) and Exhibit 2 (Tulsa, Oklahoma). In Charlotte, North Carolina, as of December 2018, the median sales price of a home was $236,750 wherein in Tulsa, Oklahoma the Q4 2018 median sales price of a home was roughly $160,000. Under the proposed rule's increase to the exemption, the vast majority of home purchases in these and other markets would not need an appraisal.[57]

Given current market realities, there is no sound reason to increase the *de minimis* exemption. However, in the alternative, the agencies should consider an approach that takes into account regional home pricing variations. As seen in the data, pricing for residential real estate varies widely based on geographic locale. A flat increase in *the de minimis* exemption entirely ignores this regional variation, but a *de minimis* exemption based on regional variation would not. Under a regional approach, in some areas the *de minimis* exemption might be lowered below $250,000, or otherwise adjusted to reflect the relative pricing conditions of residential real estate. The Appraiser Organizations believe the agencies should, at a minimum, consider this alternative approach instead of the current proposal of a 60 percent increase to the *de minimis* exemption throughout the United States.

V. Raising the *De Minimis* Exemption Will Also Impact Non-Federally Related Transactions (Addressing Question 10).

It is the assessment of the undersigned Appraiser Organizations that the proposed rule will also limit the number of appraisals for non-federally related transactions. The agencies'—

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[55] 83 Fed. Reg. at 63,117.

[56] National Association of REALTORS, *Median Sales Price of Existing Single-Family Homes for Metropolitan Areas* (Q3 2018), https://www.nar.realtor/sites/default/files/documents/metro-home-prices-q3-2018-ranked-median-single-family-2018-11-01.pdf.

[57] Recent data released by the Federal Housing Finance Agency demonstrates the wide regional and urban versus rural differences in the price of the land on which residential housing is built. *See, Detailed data show the value of land under homes across the country*, WASHINGTON POST, (Jan. 23, 2019), https://www.washingtonpost.com/us-policy/2019/01/23/why-its-problem-that-dirt-brooklyn-is-so-much-more-expensive-than-dirt-arkansas/?utm_term=.21814a31f5d8.

the prudential regulators of lenders and other market participants—decisions carry significant weight for the residential real estate industry. Enactment of the proposed rule will fundamentally alter the approaches of lenders and other market participants in their assessment of the necessity of the appraisal for non-federally related transactions. Specifically, in response to an increase in the *de minimis* exemption from $250,000 to $400,000 for federally-related transactions, a lender will likely raise its own internal *de minimis* exemption, limiting appraisals to residential real estate transactions above the newly established $400,000 threshold. This may not be the intent of the proposed rule but will be an unintended consequence. In addition, it will signal to lenders and purchasers that the prudential regulators do not view appraisals as a valuable asset to the home valuation process, and instead, demonstrates an increasing favoritism towards the deregulated and uncertain evaluation model. The Appraiser Organizations note, for example, the increasing role of non-financial institution mortgage lenders and brokers in mortgage originations. These originators may have competitive incentives to substitute evaluations for appraisals at transaction price levels for which appraisals would not be required in a federally-related transaction.

This proposed rule comes on the back of other federal regulations that have sought to further chip away at federal appraisal requirements. In particular, in September 2017, the GSEs, Fannie Mae and Freddie Mac, at the direction of the Federal Housing Finance Agency, expanded their GSE appraisal waiver program, due, in part, to an increase reliance on AVMs.[58] In response to the Fannie Mae and Freddie Mac regulations, many lenders began shifting their policies and procedures to expand use of AVMs and further limit their use of traditional appraisals. This shift includes the use of "hybrid" appraisals in which non-appraiser third parties inspect and/or photograph a property and an appraiser then conducts a desk appraisal using that information.

Therefore, it is the position of the Appraiser Organizations that raising the *de minimis* exemption will also limit the number of non-federally related transaction appraisals. In their proposed rules, the agencies do not contemplate this potential consequence, and we respectfully request, prior to the passage of the proposed rule, the agencies analyze the possible ramifications of their rules on non-federally related transactions.

VI. Evaluations are Inadequate Protections for Consumers and Lenders in Rural Areas and the Agencies Should Encourage Lenders to Minimize Situations in Which the Prerequisites for the Statutory Exemption Would Arise (Addressing Question 12).

Rural properties can have a unique heritage and layout, which may be inadequately documented. There is often a lack of readily available data, not only on the property to be

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[58] Federal Housing Finance Agency Office of Inspector General, *An Overview of Enterprise Appraisal Waivers*, Sept. 14, 2018, https://www.fhfaoig.gov/Content/Files/WPR-2018-006.pdf.

appraised, but of their market in general. As a result, rural properties require complex valuations that necessitate engagement of a skilled professional appraiser who would have the competence and geographic knowledge to complete such an assignment, providing a solid foundation for a successful lending and purchasing decision. For example, it may make a significant difference to the value of a property as collateral if the "lake" on the adjacent property is a stocked trout pond or a hog farm's waste disposal lagoon. Determining how much of a difference, in a particular rural geography, requires the judgment of a certified/licensed appraisal professional applying USPAP standards and ethical responsibilities. Appraisals made by appraisal professionals would provide similarly valuable consumer protection to purchasers to avoid overpaying for a property.

In contrast, as set out in Section II, evaluations may be conducted by untrained individuals with potential conflicts of interest—who would be especially susceptible to making valuation errors in a complex rural environment. Moreover, an AVM used to assist in an evaluation could well be inherently misleading if the number of recent transactions used to assess the market is too few to permit a statistically useful sample size while incorporating inadequate property data to permit a determination as to what transactions, if any, are actually comparable.

While the rural exemption is specified by section 103 of Public Law 115-174,[59] and, as the NPRM notes, its proposal merely adds the statutory exemption to its list of regulatory exemptions, the Appraiser Organizations believe that use of the rural exemption may be based on an artificial claim of an "appraiser shortage." In particular, an evaluation may be used if, *inter alia*, "the mortgage originator or its agent, directly or indirectly—

> (A) has contacted not fewer than 3 State certified appraisers or State licensed appraisers, as applicable, on the mortgage originator's approved appraiser list in the market area …; and
>
> (B) has documented that no State certified appraiser or State licensed appraiser, as applicable, was available within 5 business days beyond customary and reasonable fee and timeliness standards for comparable appraisal assignments, as documented by the mortgage originator or its agent….[60]

The experience of members of the Appraiser Organizations, is that where lenders use the services of third parties, i.e., AMCs, those organizations depress the fees actually paid to appraisers, with the result that appraisers with the requisite rural appraisal and geographic competence will not respond to requests for such appraisals—creating an artificial documentation of the statutory "shortage." In contrast, if lenders were to work directly with appraisers to develop their own panels of appraisers with rural competence in the relevant market

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[59] 12 U.S.C. § 3356(b).
[60] *Id.* at § 3356(b)(2).

areas, based on knowledge of those appraisers' fee schedules, those lenders would more likely be able to identify appraisers willing and able to provide the appraisal in a timely manner.

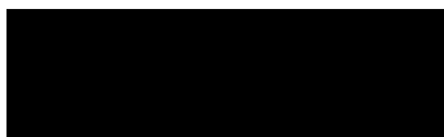
Thus, the Appraiser Organizations believe that, if the agencies incorporate the statutory reference in the regulation's exemption listing, they also should provide guidance to lenders that they engage in direct outreach to appraisers with rural competence. This requirement would facilitate the availability of appraisers willing to undertake such engagements. Such prior outreach should be a prerequisite to invoking the statutory shortage conditions with respect to an individual transaction. By setting out such guidance, the agencies will help ensure that inadequate evaluations are not needlessly substituted for appraisals that provide necessary consumer and prudential protections.

CONCLUSION

The Appraiser Organizations believe that, for the reasons set out above, the NPRM's proposal to increase the *de minimis* exemption to $400,000 should not be adopted. The NPRM attempts to justify increased use of evaluations as a cheaper-faster means of *ordering* valuations. Such a justification disregards the Dodd-Frank Act's consumer protection mandates and puts at risk the very low-income and first-time buyers who most deserve the informational benefits and USPAP assurances that appraisals provide. Moreover, the agencies' efforts to reduce the number of required appraisals is part of a misguided effort to deal with a claimed appraiser shortage by reducing appraisal demand. Such efforts could more appropriately be focused on agency outreach to the lender and appraiser communities to better understand potential concerns over cost and time for home valuations.

The Appraiser Organizations further request that a hearing be held to more fully explore these issues prior to the agencies finalizing this rulemaking proceeding. As set out above, alternatives that could be considered include developing regional *de minimis* standards that reflect the wide variations of median home prices, for example, among metropolitan areas and between urban and rural parts of a state.

Very truly yours,



W. Stephen Cannon
Richard O. Levine
James J. Kovacs

EXHIBIT 1

Market Overview

Key metrics by report month and for year-to-date (YTD) starting from the first of the year.

Charlotte Regional Realtor® Association

Key Metrics	Historical Sparkbars	12-2017	12-2018	Percent Change	YTD 2017	YTD 2018	Percent Change
New Listings	12-2016 12-2017 12-2018	2,722	**2,601**	- 4.4%	60,049	**59,889**	- 0.3%
Pending Sales	12-2016 12-2017 12-2018	2,768	**2,769**	+ 0.0%	49,169	**48,225**	- 1.9%
Closed Sales	12-2016 12-2017 12-2018	3,692	**3,176**	- 14.0%	49,072	**47,745**	- 2.7%
List to Close	12-2016 12-2017 12-2018	100	**101**	+ 1.0%	97	**93**	- 4.1%
Days on Market Until Sale	12-2016 12-2017 12-2018	50	**50**	0.0%	47	**42**	- 10.6%
Cumulative Days on Market	12-2016 12-2017 12-2018	60	**58**	- 3.3%	56	**50**	- 10.7%
Average List Price	12-2016 12-2017 12-2018	$283,999	**$298,038**	+ 4.9%	$307,082	**$319,915**	+ 4.2%
Average Sales Price	12-2016 12-2017 12-2018	$279,913	**$282,894**	+ 1.1%	$269,630	**$286,796**	+ 6.4%
Median Sales Price	12-2016 12-2017 12-2018	$233,000	**$236,750**	+ 1.6%	$224,900	**$238,000**	+ 5.8%
Pct. of Original List Price Received	12-2016 12-2017 12-2018	96.3%	**95.8%**	- 0.5%	96.9%	**96.9%**	0.0%
Housing Affordability Index	12-2016 12-2017 12-2018	107	**100**	- 6.5%	111	**100**	- 9.9%
Inventory of Homes for Sale	12-2016 12-2017 12-2018	9,268	**8,718**	- 5.9%	--	**--**	--
Months Supply of Homes for Sale	12-2016 12-2017 12-2018	2.3	**2.2**	- 4.3%	--	**--**	--

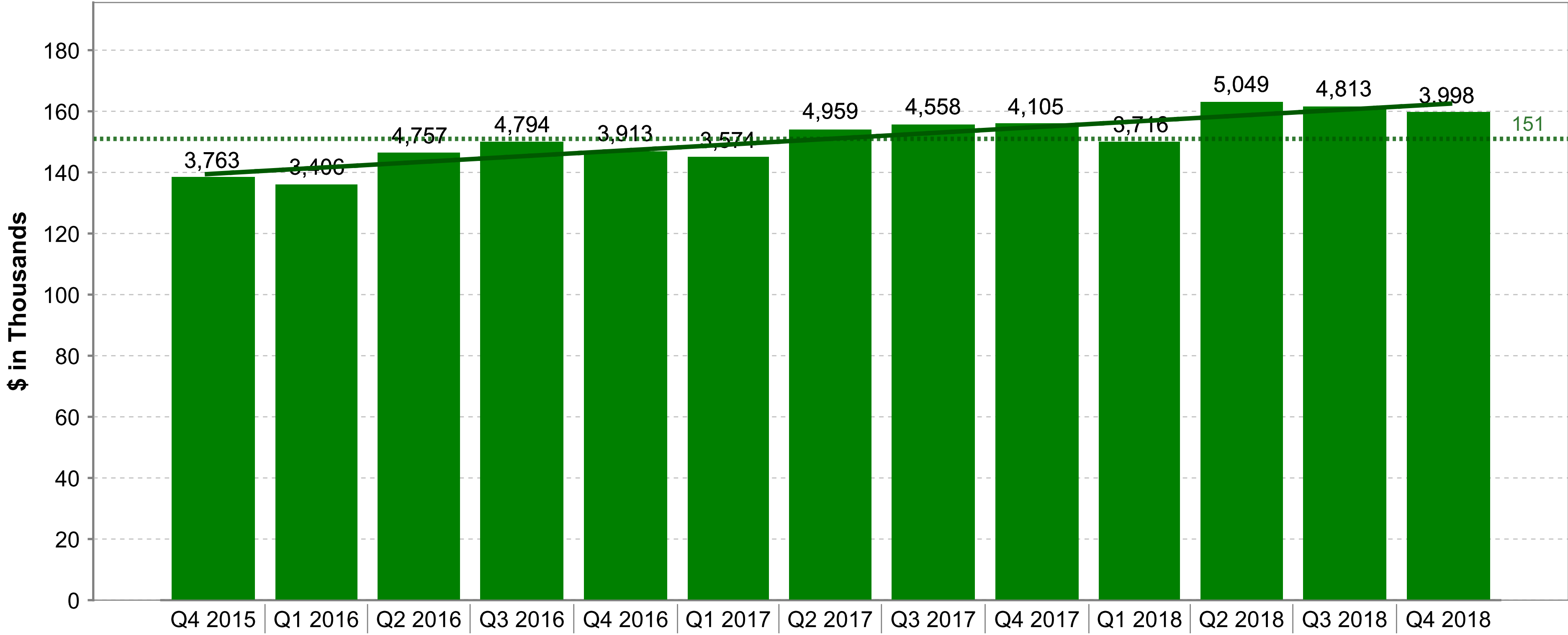
EXHIBIT 2

Market Dynamics

Thomas E. Allen Appraisals, LLC

Median Price (Sold)

3 Years (Quarterly) Q4 2015 - Q4 2018



Sold

KEY INFORMATION

	Quarterly Change	Quarterly % Change	Total Change	Total % Change
Sold	1,921.64	1.38	23,059.66	16.54

Sold
+16.5%

MLS:	GTAR	Period:	3 Years (Quarterly)	Price:	All	Construction Type:	All	Bedrooms:	All	Bathrooms:	All	Lot Size:	All
Property Types:		Residential: (House)										Sq Ft:	All
All MLS:		Greater Tulsa Association of REALTORS®											

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Market Dynamics

Thomas E. Allen Appraisals, LLC

Median Price (Sold)

3 Years (Quarterly) Q4 2015 - Q4 2018

	FOR SALE		UNDER CONTRACT		SOLD		EXPIRED		NEW LISTINGS	
Time Period	Median $	# Properties	Median $	# Properties	Median $	# Properties	Median $	# Properties	Median $	# Properties
Q4 2018	186,500	12,855	159,900	3,749	159,685	3,998	220,000	3,280	175,000	5,622
Q3 2018	185,000	14,759	164,500	4,533	161,500	4,813	215,000	2,993	175,900	7,706
Q2 2018	181,917	14,651	165,000	5,019	163,000	5,049	199,000	2,579	176,900	8,406
Q1 2018	179,000	13,577	159,900	4,496	150,000	3,716	195,350	2,836	174,900	7,192
Q4 2017	178,914	13,170	155,000	3,570	156,000	4,105	209,900	3,215	169,000	6,002
Q3 2017	178,900	14,692	159,500	4,489	155,692	4,558	205,000	3,035	169,900	7,632
Q2 2017	176,900	14,455	159,900	4,804	154,000	4,959	194,500	2,591	170,000	8,152
Q1 2017	169,900	13,492	150,000	4,420	145,000	3,574	184,900	2,769	168,000	7,411
Q4 2016	169,000	12,304	149,000	3,269	146,900	3,913	197,000	2,954	159,000	5,457
Q3 2016	169,000	14,106	149,964	4,447	150,000	4,794	190,000	2,812	159,900	7,187
Q2 2016	165,000	14,330	150,000	4,884	146,500	4,757	169,900	2,526	160,000	8,114
Q1 2016	159,500	13,245	144,900	4,228	135,950	3,406	174,900	2,801	159,900	6,889
Q4 2015	155,000	12,591	139,900	3,382	138,500	3,763	174,900	2,853	149,900	5,482

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