

September 20, 2002

Office of the General Counsel
Regulations Division
Room 10276
Department of Housing and Urban Development
451 Seventh Street, SW
Washington, DC 20410

COMMENTS RE: DOCKET NO. FR-4744-A-01

The **NATIONAL ASSOCIATION OF REALTORS**[®] (NAR) representing over 810,000 real estate practitioners, of which 30,000 are appraiser members, would like to submit the following comments on the Advance Notice of proposed rule making for the FHA Appraiser Watch Initiative [Docket No. FR-4744-A-01, July 23, 2002]. These comments are in addition to the joint comments submitted in conjunction with the Appraisal Institute and the American Society of Appraisers. NAR agrees with HUD's assessment that Appraisers and Appraisals play a critical role in regards to the FHA-insured loan portfolio. We also recognize the need for HUD to ensure the competence of their Roster Appraisers and to effectively monitor their performance in order to ensure their competency. We agree that accurate, competently prepared and professional appraisals are vital to the success of the FHA Single Family Mortgage Insurance Program and the integrity of the FHA Insurance fund.

NAR agrees with the suggestion made by HUD to use a performance-based rating system to evaluate the appraisers on the roster. However, the basis of the performance criteria proposed by HUD, defaults and claims, is a point of major disagreement.

Defaults and Claims Cannot be used as Performance Indicators for Appraisers

FHA Roster Appraisers are required to complete appraisals on properties to determine the property's eligibility for mortgage insurance on the basis of its condition and location and to estimate the value of the property for mortgage insurance purposes. Appraisals and appraisal reports must be prepared in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP) and supplemental standards required by HUD and FHA. The qualifications of the borrower, their credit history, their debt history and their history of employment and income is not considered by the appraiser and has no bearing whatsoever on the appraiser's opinion of value or the eligibility of the subject property for mortgage insurance. Nowhere in USPAP or in HUD Handbook 4150.2 are these factors described as being required to be considered as part of the appraiser's analysis of the property, its marketability or its value.

FHA Roster Appraisers provide an opinion of the value of real property and make a determination as to its compliance with HUD's Minimum Property Standards. They do not service the loan, collect monthly mortgage payments and have no idea who is current, when payments are late, or when a mortgage loan is being foreclosed. The fact that a borrower fails to

make loan payments does not mean the house is worth any less than the appraiser's estimate.

HUD makes two statements with seemingly reasonable suppositions in laying the groundwork for the Advance Notice of proposed rule making:

“Just as a consistently higher level of poor underwriting is reasonably expected to be linked to a consistently higher level of defaults, a consistently higher level of poor appraisals may be associated with a consistently higher level of defaults, regardless of the quality of the underwriting” and “ While poor underwriting practices also increase the probability of defaults and claims, it is reasonable to conclude that at some point, a high enough rate of defaults and claims on loans secured by properties appraised by an appraiser is indicative of inadequate performance.”

Regardless of the reasonableness of these suppositions, nothing is offered as evidence, anecdotal or otherwise, to support these hypothesis. There have been many recent news stories and articles citing other reasons for defaults such as the downturn in the economy, increases in unemployment, the sluggish recovery from last year's recession and the proliferation of new loan products, many of which were designed to help increase the homeownership rate and have not been "stress tested" in a recession before. None, however, has alleged appraiser responsibility for mortgage loan default and foreclosure.

HUD Should Not Issue Proposed Regulations Relative to the Appraiser Watch Initiative

HUD wants to establish a clear, consistent and familiar standard and procedure for an appraiser to maintain status on, or be removed from, the FHA Appraiser Roster. NAR shares this goal with HUD, but disagrees that the Appraiser Watch Initiative is the way to achieve this objective. As we indicated in our joint comment letter with the Appraisal Institute and the American Society of Appraisers, we would strongly encourage HUD not to go forward with the Appraisal Watch Initiative because of the following reasons which are expounded upon in the joint comment letter:

1. Loan defaults are caused by factors beyond the control of the appraiser.
2. Appraiser Watch does not address poorly performing appraisers whose appraised loans do not end up in default.
3. Appraiser Watch does not establish a system of proximate cause for default.
4. Appraisers, loan officers and underwriters have different functions; therefore, their performance should not be based on the same criteria.
5. There may be unintended consequences of a default-based Appraiser Watch system.
6. Appraiser Watch does not address lender accountability for appraisals.
7. Appraiser Watch fails to address inappropriate client pressure on appraisers.
8. Appraiser Watch fails to address historical failures of HUD management systems.
9. HUD's elimination of the Appraisal Quality Assessment (AQA) process appears not to have been justified.
10. Appraiser Watch fails to curb appraisal problems before they occur.

Additional Considerations and Requests for Comments

In regards to the issues raised in the Advance Notice of proposed rule making NAR provides the following comments:

1. Whether HUD should establish a minimum number of appraisals as a threshold for any action, and if so, what number would be appropriate?

It is important that the sample is statistically significant and not skewed by an insufficient number of appraisal assignments from which to draw conclusions. The benchmark should be at least the average number of FHA Appraisal Assignments completed by appraisers for a twelve-month period in a particular market or served by Homeownership Center. In no case should this amount be less than 60 appraisals.

HUD may find it more productive to examine the work product of “high volume” FHA Appraisers. Anecdotal evidence suggests there are a few appraisers receiving an unusually high number of FHA appraisal assignments over an extraordinarily large geographic area. In some situations, a close examination of the assignments and the location of the properties might reveal the physical impossibility of the Roster Appraiser being able to personally complete the work. Many appraisers allege these “high volume” appraisers use non-roster trainees to make the site visit, inspect the subject property and prepare the appraisal report for the Roster Appraiser. A specific example of this situation is detailed in our joint comment letter with the Appraisal Institute and the American Society of Appraisers.

2. Whether HUD should specify the age of loans secured by appraised properties that would be considered under a standard, and what loan age would be appropriate (e.g., appraisals for loans not more than one, two or three years old, measured from the time of origination).

The peak time for delinquencies is usually two to three years after borrowing. The focus should be on appraisals less than three years old.

3. Whether a higher or lower rate than the 200 percent used in Credit Watch would provide an adequate measure of appraiser performance and level of protection for FHA.

Until HUD is able to provide data indicating a causal link between appraiser performance and defaults and claims, any ratio is purely arbitrary.

4. What period of time over which appraisals are conducted should be used for evaluation purposes (e.g., performance over 12 months, or 18 months, or 24 months)?

Again, until HUD is able to provide data indicating a causal link between appraiser performance and defaults and claims, any time period is purely arbitrary.

5. What factors in addition to the rate of loan defaults and FHA insurance claims should HUD consider in evaluating appraiser performance?

Appraiser performance should be evaluated on the basis of their compliance with USPAP.

Performance standards specific to HUD-FHA requirements should be evaluated on the basis of

compliance with the standards specified in the HUD Handbook 4150.2. The most effective means of evaluating this performance is

by independent reviews of representative, randomly selected samples of a Roster Appraiser's work product. These reviews should be personally completed by local market (not regional), Roster Appraisers with five or more years of FHA appraisal experience. The FHA Roster Appraisers must be provided copies of the reviews in order to correct deficiencies or shortcomings in their practice. In the event of serious deficiencies, remediation or removal from the roster may be required. Also, when appropriate, HUD must refer deficient Roster Appraisers to the appropriate State Regulatory Agency for investigation and possible disciplinary action.

6. Should the severity of loss be considered as a factor in evaluating an appraiser's performance?

No. The severity of loss is subject to a multitude of factors well beyond the control and responsibility of the Roster Appraiser. Loss could be dramatically increased due to the borrower's abuse of the property, failure to maintain the improvements, willful damage to the improvements as revenge for foreclosure and vandalism. Changes in market conditions and the local economy after the completion of the appraisal could increase the loss. The severity of loss could be affected by interest rates or the ability of the HUD contractor responsible for disposition.

Each of these is well beyond the control of the Roster Appraiser. Rating the appraiser on the severity of loss adds insult to the injury of rating their performance on defaults and claims; factors outside the realm of their influence.

7. If included as a factor, how should severity of loss be considered in evaluating performance?

As indicated in our previous answer, severity of loss should not be included in evaluating performance.

8. What kinds of factors should be considered as mitigating for an appraiser with higher than normal defaults and claim rates (e.g., factors beyond the appraiser's control)?

As we mentioned in the beginning of our comments, mitigating factors would include the appraiser not having access to the borrower's credit report, the borrower's payment history and the borrower's history of employment. These mitigating factors would also include the level of training the appraiser is required to have in mortgage loan underwriting and the fact the appraiser does not make the lending decisions.

9. How much time should be provided for an appraiser to request an informal conference after receiving notification of proposed removal (e.g., 15, 30, or 45 days)?

At least 45 days should be allowed in order to provide enough time to prepare the proper response.

10. What is an appropriate period of removal from the roster before a reinstatement is permitted?

Appraisers should not be removed from the roster unless it is found they have not performed according to USPAP and the requirements stated in the HUD Handbook 4150.2. The level of

sanction should depend upon the severity of the offense because removal from the roster might not be warranted in every case. In each case where a violation of USPAP or failure to follow the Supplemental Standards required by HUD-FHA is alleged, a referral of the alleged offender to the appropriate State Regulatory Board should be made.

11. What are appropriate procedures and factors to consider for reinstatement?

HUD regularly provides training for Direct Endorsement Underwriters across the country and our assumption is that this training is offered to help them adhere to HUD standards, enhance the quality of the HUD Mortgage Insurance portfolio and to minimize the likelihood of mortgage loan defaults, foreclosures and claims. Appraisers, as HUD's eyes, ears and evaluators, would benefit from periodic training and regular (biennial at least) re-certification of their competency. State Regulatory Boards routinely place offenders on probation and require remedial training.

Although FHA Appraisal standards are stringent, HUD has left it to the private sector to inform Roster Appraisers of the specific criteria and requirements of their appraisals. To our knowledge, HUD has not provided any training to these trainers and thus has no assurance of the quality of the training. Professional associations and private schools have only published manuals and postings of "frequently asked questions" for use in the development of their course materials. Again, to our knowledge, no professional associations or private schools have been provided access to the Real Estate Assessment Center's Knowledge Base to alert potential Roster Appraisers of the "real world" problems encountered daily by Roster Appraisers. If the goal is to ensure Roster Appraisers are fully competent to prepare appraisal reports and the HUD required addenda, much more in the way of guidance and information must be provided to the private education providers.

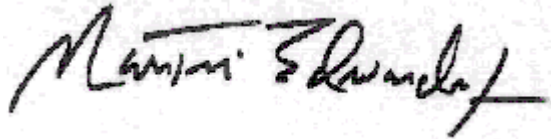
As a means of ensuring the excellence and integrity of the appraisers listed on the roster, NAR recommends that HUD require two years as a licensed or certified appraiser as a condition of being placed on the FHA Appraisal Roster. Appraisals completed for HUD/FHA are often more complicated than those completed for conventional clients and thus warrant the additional experience. In comparison to conventional appraisals, FHA appraisals require a higher degree of skill and more knowledge of construction, depreciation, cost estimating for repairs and estimating the useful and remaining life of residential improvements and equipment.

Conclusion

As a final comment, NAR is concerned that the Appraiser Watch initiative will virtually require Roster Appraisers to "red line" or accept appraisal assignments only when they are certain that the borrower will not default. In other words, will the end result of this initiative be higher quality appraisals, or will it have the unintended consequence of forcing Roster Appraisers to elect not to subject themselves to consequences and possible discipline for circumstances over which they have no control? Many worthy buyers, particularly first time homeowners, may be effectively foreclosed from ever achieving the dream of homeownership. Again, we would like to reiterate that HUD should not proceed to issue proposed regulations on the Appraisal Watch initiative.

NAR appreciates the opportunity to provide these comments and if we can provide further information please let us know.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Martin Edwards, Jr.", written in a cursive style.

Martin Edwards, Jr., CCIM, CIPS
President