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U.S. Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410

RE: 2003-2008 HUD Strategic Plan

To Whom It May Concern:

On behalf of the more than 25,000 members of the Appraisal Institute and the American Society of Appraisers, we thank you for the opportunity to comment on the draft of HUD's FY 2003-2008 Strategic Plan. Our members, who comprise the leading professional organizations of appraisers in the United States, are very concerned about the Strategic Plan's goals regarding HUD's appraisal policies.

We are pleased HUD has recognized the need for improvement in its handling of appraisals in general, and within its Federal Housing Administration (FHA) Office of Single Family Housing, in particular. It is encouraging to see that the need for appraisal management improvement is acknowledged within the Strategic Plan's goals of increasing homeownership opportunities; embracing high standards of ethics, management and accountability; and fighting practices that permit predatory lending. HUD is heeding the advice given during July 24, 2002 testimony provided by Stanley Czerwinski, Director of Physical Infrastructure Issues of the Government Accounting Office, wherein he stated that HUD needs to "improve, among other things, its oversight of lenders and appraisers."

The importance of traditional appraisals in federally-related mortgage transactions is as vital as ever, if not more so. With lower down-payments and new down-payment assistance programs proliferating—enabling many potential home buyers the opportunity to purchase homes who, in the past, would have been considered too great a risk—a very significant emphasis is placed on the collateral score of the property in question. If inaccurate appraisals are permitted to go unchecked, FHA insurable mortgage loans are put in dangerously high risk positions.

The key appraisal points HUD's Strategic Plan hits upon are the need for "better monitoring of appraisals" combined with new protocols for accomplishing that monitoring; "strengthening licensing/certification for appraisers on the FHA Appraiser Roster"; and "requiring lenders to exercise more oversight of appraisers they employ." These general goals are laudable. What we intend to do in this comment letter is offer specific suggestions as to how HUD can accomplish these goals.

Suggestion 1: Protect homebuyers from unscrupulous lending practices by ensuring the buyers' ability to see the fee for an appraisal itemized on their Good Faith Estimates.

HUD's Strategic Plan's goal of increasing homeownership opportunities includes fighting practices that permit predatory lending. We believe HUD should conduct a thorough analysis of its currently proposed rule of the Real Estate Settlement Procedures Act (RESPA) in relation to that goal.

Under the proposed RESPA rule, the "bundling" of various closing costs, including appraisals, would be acceptable on the Guaranteed Mortgage Package (GMP). However, we see this type of packaging as further cause for concern over proper disclosures being made available to consumers. It is important to establish safeguards to protect homebuyers from unscrupulous players in the residential real estate market, and this particular provision in the proposed rule may actually hurt existing consumer protections. Under a GMP, consumers would have no way of knowing what they are paying for at closing. It would be clouded as to what fees are being paid and to whom. While this may "simplify" the process for the lender, the borrower's fees would be obscured. And after all, it is the borrower whom RESPA is attempting to protect.

Therefore, we recommend that HUD keep the actual contract appraisal fee under the Good Faith Estimate (GFE) and out of the GMP. We recommend that only the lender's charge for reviewing or administering the appraisal function should be included in the GMP, not the actual amount paid to a contracted appraiser. We recommend the fee that is paid to the contracted real estate appraiser not be included with application, origination and underwriting services and any other lender-required services or other fixed fees. Instead, we recommend the contracted appraiser fee be excluded from the GMP as are costs for hazard insurance, per diem interest, and escrow deposits.

This suggestion would allow the contracted appraiser to be considered an entity outside of the GMP package. It is our view that GFE disclosure is adequate for consumers, especially if the costs are itemized. Under these circumstances, the consumer could be given a copy of the contracted appraiser's invoice at closing to document the actual cost of service. Lender fees for appraisal administration or review would then be transparent, and could subsequently be compared to the quotes in the GMP package. We feel implementing this suggestion would greatly assist in HUD's goal to diminish predatory lending practices.

Suggestion 2: Improve communications with the appraisal community.

The last year has witnessed a great deal confusion and anxiety among HUD contractors—appraisers and lenders alike—caused by a deficiency in clear communication on the part of HUD in relation to its appraisal policies. While the lack of clarity is not a new phenomenon, many of our members feel it has been magnified over the last year due to the proposed rule on the Appraiser Watch initiative. Many felt that the dismantling of the Real Estate Assessment Center's (REAC's) Single Family Appraisal Subsystem (SASS) system was not justified. Moreover, no correspondence from HUD has offered up any current alternative to SASS. Questions addressed to HUD asking how the appraisal review process and sanctioning matrix are being maintained have been met with silence.

HUD will benefit from giant gains in its credibility if it chooses, as one of its strategic plans, to rectify this non-communication. One manner in which to accomplish this would be to hold regular meetings at the local level with its appraiser contractors to engage in on-going dialogues with the appraisal community.

Along these lines, HUD should contemplate launching a more consistent exchange with professional appraisal organizations, as these bodies bring a great deal of insight and experience to these issues.

In addition, HUD should consider creating a new clear and concise document which consolidates all its appraisal guidelines. This document would address all aspects in which HUD deals with appraisals. In general, all procedures, requirements and standards would be clearly stated. Specifically, the acceptance, monitoring, reviewing, disciplining and removal of appraisers would be detailed and defined simply and precisely.

Over the years, HUD has issued various texts dealing with appraisals. Yet the discrepancy between the release dates of these documents, coupled with their obscurity, make it extremely difficult for both FHA appraisers and users of appraisal services to keep fully abreast of what those guidelines are. For example, Mortgagee Letter 94-54, Mortgagee Letter 99-35, and HUD Valuation Handbook 4150.2 could all be merged into one well-organized topical document. As new rules and procedures are put forth, each would be added to the main document. This would allow not only FHA appraisers, but anyone affected by the appraisal process—lenders, brokers, realty agents and consumers—to have one place to which to refer in order to learn about HUD's appraisal systems and policies.

Suggestion 3: Accomplish better monitoring of appraisals and appraisers through improvement of HUD management systems; reviewing appraisers based on the quality of appraisals; and addressing high-volume appraisers.

HUD states in its Strategic Plan that it intends to "establish an Appraiser Watch system to measure the performance of individual appraisers," based on the model of the successful Credit Watch program which currently oversees FHA lender performance. If HUD intends to establish such a program, it is vital that when it does so that it integrates its existing monitoring systems along with it. In addition, per the advice of the GAO found in Stanley Czerwinski's Congressional testimony last July, it needs to employ people with the right skills in the right places to monitor its contractors—in this case, appraisers.

There is no doubt that proper monitoring of poorly performing appraisers in badly needed. Establishing an Appraiser Watch program which is comparable to Credit Watch in spirit (that is, that it oversees/monitors FHA contractors) is a worthy goal. However, accomplishing the goal by duplicating Credit Watch's methodology based on default rates is not. Assessing appraisals based on the performance of loans is faulty reasoning. An honest appraiser cannot predict the actions of a potential home buyer. He/she can, however, provide an objective and straightforward estimate of value for a property. If an appraisal is inflated, it may not necessarily end up in the FHA borrower defaulting. It can, however, ultimately skew the home values of an entire neighborhood and contribute to wider economic crises.

Therefore, we recommend that monitoring of appraisers is accomplished in two ways: reviewing appraisers based on the quality of their appraisals, and addressing high-volume appraisers. Reviewing appraisals need not be a tedious process any longer with today's technological advancements. Current technology enables the flagging of potentially inaccurate appraisals to be cost-effective and time-efficient. Custom automated review systems remove bias and allow for quick, consistent and thorough reviews. Where an automated system finds a discrepancy, the appraisal is flagged as potentially inaccurate and is recommended for manual underwriting, where inaccuracies and/or potential standards violations would be confirmed or disproved.

"High-volume" appraisers typically are FHA-approved appraisers who have "trainees" (who are not approved for the FHA Appraiser Roster) perform interior inspections of homes and then the FHA appraisers themselves sign the reports as if they'd inspected the homes themselves. According to recent information provided by the Atlanta Home Ownership Center (HOC), where this problem appears to be common, many of these appraisers had performed in excess of 1,000 appraisals in a given year (almost 3 appraisals per day for 365 days). This is a clear violation of HUD's appraisal policies. Just as inaccurate appraisals need to be flagged, so, too, should questionable appraisers not be able to slip through the system.

Suggestion 4: Strengthen professional credentials of appraisers on the Appraiser Roster by removing unqualified appraisers from the Roster; increasing FHA education/qualifications requirements; and improving HUD staff training.

On January 29, 2002, our organizations submitted comments to HUD regarding the Proposed Rule on Appraiser Qualifications for Placement on the FHA Single Family Appraiser Roster. While we acknowledged the proposed actions are a step in the right direction, we are still concerned that there remain on the Roster appraisers who are in fact not qualified to be on it. HUD needs to address this problem to ensure that only qualified appraisers are performing assignments for FHA. HUD needs to include in its Strategic Plan, and within the appraisal document we recommend it create mentioned above, a methodical manner in which to remove the unqualified appraisers in order to maintain the integrity of the Roster and the FHA mortgage loan program itself.

Indeed, one vital manner in which to improve the quality and accuracy of FHA appraisals is through establishing higher standards for qualification. HUD must strive to have the most qualified and experienced appraisers performing appraisals on its behalf. We suggest the test for acceptance on the Roster be modified to raise standards to ensure that only highly qualified and experienced appraisers are accepted. We also suggest HUD periodically recertify and/or reevaluate appraisers on the FHA Appraiser Roster. Just as an appraiser has to recertify with a state appraiser board periodically, appraisers approved on the Roster should recertify their qualifications.

Recertification training would also give HUD the opportunity to interact with appraisers regarding various updates and possible concerns with the operation of the program. There are many particulars entailed in the generation of FHA appraisals. Distribution of HUD/FHA appraisal materials and one-on-one contact with the contractors will allow FHA appraisers the benefit of agency-specific education, so critical to the efficient administration of the appraiser program.

HUD has made some positive steps in regards to training staff to ensure competency with appraisal issues. Courses taught by Appraisal Institute practicing appraiser members during the Summer of 2002 brought fresh perspectives to HUD staff and were very well received, with most participant evaluations designated as “Excellent.” The interaction between market players and employees improved the understanding of those in charge of overseeing the risk management of single-family mortgages insured by FHA, and should improve the operations of the HOCs. We encourage HUD to embark on these types of training projects on a more regular basis.

Suggestion 5: Require lenders to exercise more oversight of appraisers they employ by enforcing Mortgagee Letter 94-54 and compliance with HUD 4150.2 Handbook. In addition, establish strict policies regarding client pressure.

HUD will not solve the mortgage fraud/predatory lending problem until it addresses many lender-related issues. These include: 1) HUD’s holding Direct Endorsement lenders accountable for the quality of appraisals and 2) Inappropriate client pressure being placed on appraisers as a result of the Lender Select program.

In April 1999, GAO recommended that HUD determine the department’s authority to hold FHA-approved lenders accountable for poor-quality FHA appraisals performed by the appraisers they select and issue policy guidance that sets forth the specific circumstances under which HUD may exercise its authority to hold lenders accountable. HUD informed the GAO it was working on a letter to mortgagees that it believed would meet the GAO’s recommendations. Such a letter has yet to be circulated.

In fact, Mortgage Letter 94-54, published in 1994, set forth the procedures for lenders to select their own appraisers (Lender Select). Under this policy, Direct Endorsement lenders are allowed to select appraisers from the Lender Selection Roster. However, while the Direct Endorsement lenders were given the right to select their own appraisers, they were also required to accept responsibility, equally with the appraiser, for the integrity, accuracy and thoroughness of the appraisal. In addition, the Direct Endorsement lenders are also supposed to be held accountable by HUD for the quality of the appraisal.

According to HUD records, no Direct Endorsement lenders have been sanctioned because of a lack of integrity, accuracy, thoroughness or quality of an appraisal. We find this unacceptable as HUD routinely sanctions appraisers who have performed inaccurate or fraudulent appraisals. We encourage HUD to enact a rule on Lender Accountability for Appraisals and hold lenders strictly accountable for the quality and accuracy of appraisals.

Should HUD not be able to provide sufficient oversight of lenders, we suggest HUD consider eliminating the Lender Select program, replacing it with an alternative appraisal ordering system that provides true independence for the appraiser. We also believe that enforcement activity and penalties for lenders should be increased.

The 1999 Third Quarter Report of the HUD Office of the Inspector General recommended that HUD remind direct endorsement lenders that they are responsible and accountable for selecting appraisers and ordering the appraisal report on single family properties. This responsibility must be taken seriously and must not be given to anyone else. Also, if a lender can demonstrate that undue pressure from any individual or entity involved in the FHA insurance program caused the lender's business to suffer by following FHA rules, HUD should consider appropriate disciplinary action against the responsible individuals or entities. We concur with this position.

We encourage HUD to establish a system that informs appraisers of HUD's requirements relating to inappropriate client pressure on appraisers and establishes common procedures for conducting investigations of complaints issued by appraisers. Such procedures would tell the appraiser what information must be provided in the complaint and whether the appraiser's identity will be held in confidence by HUD during the investigation. HUD could even establish a "hotline," or clearly specify a staff member who could handle such investigations and make this known to appraisers on the FHA Appraiser Roster. HUD, when receiving these complaints, should provide sufficient resources to conduct thorough investigations and conduct effective enforcement activities.

Conclusion

The Appraisal Institute and the American Society of Appraisers commend the goals HUD has established regarding appraisal policies in its 2003-2008 Strategic Plan. We hope that the specific ideas outlined above will be taken into consideration and will aid HUD in its challenge to implement its goals in realistic, tangible and attainable ways.

Should you have any questions, please contact Don Kelly, Vice President of Public Affairs, Appraisal Institute at 202-298-5583 or dkelly@appraisalinstitute.org, or Ted Baker, Executive Vice President, American Society of Appraisers at 703-733-2019 or tbaker@appraisers.org.

Sincerely,

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