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Regulations Division
Office of General Counsel
Room 10276
Department of Housing and Urban Development
451 Seventh Street, S.W.
Washington, D.C. 20410-0500

Re: Docket Number FR-4744-A-01
FHA Appraiser Watch Initiative

On behalf of the more than 30,000 members of the Appraisal Institute, American Society of Appraisers, and National Association of Realtors, we would like to thank you for the opportunity to provide comments on the Department of Housing and Urban Development's (HUD) Proposed Rule to implement an Appraiser Watch Initiative. The Appraisal Institute, American Society of Appraisers, National Association of Realtors and HUD have a long history of working together to address appraisal issues impacting our nation's housing industry. As the largest groups of real estate appraisers in the United States, we appreciate this opportunity to comment on this very important issue.

First of all, we are pleased to see HUD has reiterated the importance of real estate appraisals to HUD's mortgage insurance program. However, we believe there are inherent flaws in the Appraiser Watch Initiative that must be brought to light. We are fearful that HUD, as Stanley Czerwinski, Director of Physical Infrastructure Issues at the General Accounting Office (GAO), recently pointed out to Congress, is "only addressing the symptoms, not the root causes," regarding appraisal reforms.

The Appraiser Watch Initiative, as proposed, has raised a great deal of concern among our members, many of whom are on the Federal Housing Administration (FHA) Appraiser Roster. Most striking for our members is the fact that the new proposal would rate appraiser performance using a factor that has no direct bearing on the accuracy of the appraisal – the default rate. In addition, we have seen no evidence that the Appraiser Watch Initiative will establish an ongoing program for reviewing appraisals by using commonly accepted appraisal standards. Such programs must be used to effectively administer the current appraiser sanctions matrix.

We are disappointed the Department has focused on using default rates as a measure of the accuracy of the appraisal instead of addressing other issues that are having a negative impact on the quality of appraisals being performed for FHA. This letter seeks to point out some problems associated with using such a program to sanction appraisers. We urge HUD to address the systemic problems in its appraisal programs and abandon the Appraiser Watch Initiative. If HUD plans to attract highly experienced and educated appraisers to be involved with the FHA appraisal program, it must address the issues stated below.

Background

Through the Appraiser Watch Initiative, HUD plans to establish and monitor a performance standard that appraisers must meet to maintain their status on the FHA Appraiser Roster. Modeled after the current FHA Credit Watch Termination Initiative, Appraiser Watch is intended to provide an electronic, fully computerized monitoring system, which would permit an appraiser to be removed from the Roster if the rate of defaults and claims on closed mortgages linked to the appraiser exceeds a rate established by HUD.

Appraisals are used by HUD to determine the value of property, which in turn serves as the basis for determining the maximum insurable mortgage loan. In addition to providing an estimate opinion of value, the appraiser views the property for any observable deficiencies that may affect the health or safety of the occupants or the marketability of the property. Although the consumer oftentimes pays for the cost of the appraisal, its primary purpose is to help the lender establish a loan amount. Its secondary purpose is to identify physical problems in the property that could cause the new homeowner financial hardship immediately or shortly after entering the home.

Upon completion, the appraisal is reviewed either by a HUD staff review appraiser in the local HUD field office or by a Direct Endorsement Underwriter. The Conditional Commitment/Statement of Appraised Value, Form HUD-92800.5B, is subsequently issued, which represents HUD's estimate of value for mortgage insurance purposes. The estimate of value arrived at by the reviewer, plus closing costs and often seller contributions, is the amount on which the maximum insurable mortgage loan is determined. However, such a process may result in an inflated value, as closing costs and financing concessions do not add value to the real estate.

Following are some specific problems that we have identified in the proposed Appraiser Watch Initiative:

Problem 1: Loan defaults are caused by factors beyond the control of the appraiser

Real estate appraisers approved for the FHA Appraiser Roster provide an independent estimate opinion of value prior to the loan being made to determine the maximum amount for which the mortgage loan can be insured. However, the appraisal is not likely to be the cause of default, as the vast majority of defaults are caused by "life situations" such as illness, divorce or job loss. Appraisers do not underwrite loans. They do not approve borrowers or collect monthly mortgage payments. Appraisers see no mortgage applications and they do not check the credit records or tax returns of borrowers. In fact, the only information an appraiser typically sees is the name and address of the home being appraised. In addition, the value of a home can – and very often does – change between the time of the appraisal and the time of default. Most foreclosures occur beyond the date of the appraisal or the creation of the loan. Meanwhile, the physical condition of the home is likely to have deteriorated, particularly if the house has been abandoned or vacated at the time of foreclosure. HUD should not expect an appraisal done at one point in time to have validity at the foreclosure at a much later point in time.

HUD's Office of Inspector General (OIG) recently agreed with this position. In March 2002 the OIG commented in its 2002 Semi-Annual Report to Congress:

"We non-concurred with this proposed rule because we did not agree with removing an appraiser from FHA programs based solely on the default/claim rate of loans that the appraiser

was involved in processing. This may, inappropriately, hold the appraiser responsible for defaults that are the result of poor underwriting practices by the lender. We recommended, instead, a closer examination of the work performed by appraisers on loans with high default/claim rates. Also, the standard of over 200 percent of the default and claim rate appears to be a high standard for triggering action, considering the problems being experienced in the program. We recommended a standard that would be more inclusive of poorly performing appraisers, such as 50 percent above the norm for the area.”

Official HUD documentation also points to the fact defaults are not likely to be caused by inaccurate appraisals. According to HUD Directive Number 4566.2, *Management, Servicing and Disposition Requirements for Projects*:

“The true causes of default may be difficult to identify as they are not always apparent to the servicer. The reasons for default that surface most frequently are poor money management, over-extended obligations, loss of income, loss of employment, illness and/or a lack of concern or understanding of the mortgage obligation.”

Finally, in its report, *Mortgage Financing: Changes in the Performance of FHA-Insured Loans*, published July 2002, the GAO stated:

“Although economic factors such as house price appreciation are key determinants of mortgage foreclosure, changes in underwriting requirements as well as changes in the conventional mortgage market may partly explain the higher foreclosure rates experienced in the 1990s.”

As the GAO points out, the changes FHA’s underwriting procedures have undergone since 1995 in an effort to increase homeownership have allowed more borrowers who may not have met previous underwriting standards to qualify for loans, or have increased the amounts for which these borrowers previously could qualify. These changes, the GAO clearly states, “may have increased the likelihood of foreclosures.”

Problem 2: Appraiser Watch does not address poorly performing appraisers whose appraised loans do not end up in default

Although appraised values have very little impact on the overall default rate, this does not make them immune to contributing to mortgage problems for borrowers. Even though it is likely that other circumstances caused a foreclosure, an inaccurate appraisal can cause the property to take longer to sell and/or cause a higher loss as a foreclosure.

This problem is particularly evident when appraisers fail to report, analyze and adjust for financing and seller concessions in their appraisals. Concessions should not be mistakenly viewed by appraisers as additional value to the property. To do so would result in the lender making a loan partially secured by the creative financing of the sale. HUD currently allows up to 6 percent of concessions to be included in the loan, while charitable organizations can also build in large amounts for seller concessions. To account for these, the sales contracts can be written to include these concessions, resulting in an inflated sale price. The problem occurs when appraisers, intentionally, accidentally or under pressure from clients or other third parties, agree to support the contract price and issue a fraudulent or misleading

appraisal report. Unfortunately, if these concessions are not accounted for, a cycle of overvaluation may be created which has the capability of compounding itself.

However, a pure default-based compliance system will allow appraisers who have performed inaccurate appraisals to remain on the FHA Appraiser Roster. This is likely to occur quite frequently in cases where appraisers have not accounted for seller concessions, as many of these loans do not necessarily end in default. As long as the loans do not go into default, the appraiser can continue on the Appraiser Roster, even though the quality of his/her work may be poor. If unqualified or poorly performing appraisers are not caught, it is only a matter of time until losses occur as a result of the bad appraisals.

We understand that the Appraiser Watch Initiative is intended to supplement existing appraiser roster removal guidelines (24 CFR Part 200, Subpart G) and the appraiser sanctioning matrix found in HUD Handbook 4150.2 Chapter 7. However, it is our understanding that under Appraiser Watch, HUD will no longer perform reviews of appraisals. We have seen no evidence that the Appraiser Watch Initiative will establish a program for reviewing appraisals through an appraisal review that would review appraisals against commonly accepted appraisal standards. If this is correct, we question how HUD intends to use the existing sanctions matrix, as it depends on consistent reviews of appraisals. As proposed, HUD is sending a message that it is not concerned with the overall accuracy of appraisals.

We believe HUD has not identified unqualified and poorly performing appraisers largely because its appraisal review systems have been inadequate. Under past review systems, the review function has typically been bid out to a large firm who covers a large region and subcontracts work to local appraisers. The fees paid to the appraisers performing the reviews have been so low that many highly qualified appraisers have refused to accept these assignments. The result has been that FHA reviews, designed to catch errors in value, as well as overlooked repair items, are being completed by poorly performing appraisers. Many of these reviewers devote as little time as possible in order to justify the fees paid.

Problem 3: Appraiser Watch does not establish a system of proximate cause for default

In the Proposed Rule HUD speculates that "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." However, the Appraiser Watch Initiative does not establish whether the appraised value and/or the proper identification of repair items was or was not an issue or proximate cause of the default. The program sets no standard for establishment of proximate cause, as would be required in a court of law.

Problem 4: Appraisers, loan officers and underwriters have different functions; therefore, their performance should not be based on the same criteria

The appraiser's job is to provide an opinion of value so that FHA can determine the maximum insurable mortgage loan and to identify items that need to be repaired. A loan officer is the financial institution's representative who interviews borrowers and helps them choose the best mortgage program and fill out their loan applications. Once an application package is complete, it is forwarded to the loan underwriter, who reviews all the paperwork to determine whether the borrower and the property meet the requirements of the selected loan program that was selected.

Having a system whereby underwriters or lenders are gauged by a default threshold may make sense since the service they are providing is the loan to the consumer. However, due to the difference in function and responsibilities, it is unreasonable to evaluate appraisers based on the number of defaults. The appraiser should be evaluated on the quality of the appraisal performed.

Problem 5: Unintended consequences of a default-based system

If HUD chooses to use default rates as the sole indicator of appraisal review, the Appraiser Watch Initiative may establish a system that creates incentives for appraisers to accept appraisal assignments in low-default areas while avoiding high-default areas. We are concerned about this potential “incentive” because it may unintentionally result in the flight of highly qualified appraisers from performing assignments in high-default areas. HUD should strive to avoid this unintended consequence. Even though there is strict prohibition in commonly accepted appraisal standards against this practice, establishing a system based solely on the default rate may cause this to happen.

Problem 6: Appraiser Watch does not address lender accountability for appraisals

Even if HUD moves forward with a default-based Appraiser Watch program, HUD will not solve the mortgage fraud/predatory lending problem until it addresses many lender-related issues. These include: 1) HUD holding Direct Endorsement lenders accountable for the quality of appraisals, including strict compliance with the HUD 4150.2 Handbook and 2) Inappropriate client pressure being placed on appraisers as a result of the Lender Select program.

In April 1999, the GAO recommended HUD determine its own authority to hold FHA-approved lenders accountable for poor-quality appraisals performed by the appraisers they select. The GAO also recommended HUD issue guidance that sets forth the 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, Mortgagee 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 equal responsibility with the appraiser, for the integrity, accuracy and thoroughness of the appraisal. In addition, Direct Endorsement lenders are also supposed to be held accountable by HUD for the quality of appraisals.

According to HUD records, no Direct Endorsement lenders have yet 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. Due to advancements in technology solutions in the market, it is now possible for lenders to directly access HUD’s business rules, review appraisals electronically, flag problems for review, and be assured of compliance with HUD rules prior to closing the loan.

Problem 7: Appraiser Watch fails to address inappropriate client pressure on appraisers

Under the appraisal ordering procedures established in 1994, rather than having the appraisal (and appraiser) randomly ordered by FHA, the authority to order appraisals now resides with the originating

lender. As stated above, this change also granted the lender full responsibility for the accuracy and integrity of the appraisal, although accountability for that responsibility appears to be little enforced.

Since this modification, our organizations report that instances of client pressure have increased greatly. This, our members say, comes as a direct result of granting the appraisal ordering authority to lenders.

Under the previous "Fee Panel" system, when an appraisal was ordered, FHA would randomly select appraisers from an approved panel of appraisers. The appraiser would perform the appraisal and send it to FHA and the originating lender. Under this system, the appraiser was more insulated from most forms of pressure to deliver a predetermined value or directed report.

By contrast, under "Lender Select," the appraisal is ordered by the lender who keeps a roster of approved appraisers. Unfortunately, the power to select is also the power to influence. Through Lender Select, lenders have great influence over an appraiser to meet a predetermined value, ignore expensive and potentially deal-breaking property deficiencies, or deliver a report worded to facilitate the approval of the transaction. Fee appraisers make a livelihood on fees generated through appraisal assignments. However, our members report that many lenders make future fees contingent upon the appraiser meeting a predetermined appraised value. Should the appraiser fail to meet the predetermined value, the appraiser simply stops receiving future appraisal assignments.

Although this kind of pressure exists in all facets of the appraisal business, under the Lender Select program, the problem appears to be magnified. This kind of pressure has very specific market consequences, as lenders seek out appraisers willing to conform to lender requests. Alarming, as a result, some appraisers have been blacklisted from performing appraisal assignments. Much of FHA's appraisal work appears to be gravitating toward the least qualified and least experienced appraisers in the profession. The existence of client pressure through the Lender Select program has tended to dissuade appraisers with the highest education and experience requirements from performing FHA appraisals. A recent survey of Appraisal Institute members indicates that fewer members are performing FHA appraisals. Of Appraisal Institute members who reported performing fewer appraisals for FHA, 44 percent claim that client pressure is the culprit, which was far and away the greatest complaint. HUD must address this issue if it wants to attract experienced and highly educated appraisers to be involved in its programs.

Problem 8: Appraiser Watch fails to address historical failures of HUD management systems

Since the 1990s, the GAO has consistently found weaknesses in HUD's oversight of its single-family mortgage insurance programs. Stanley Czerwinski, Director of Physical Infrastructure Issues, testified on July 24, 2002, before the Senate Banking Committee on HUD Management Challenges, saying that HUD needs to "improve, among other things, its oversight of lenders and appraisers." And while over the last five years HUD contractors increased by 60%, HUD has continued to experience a shortage of trained and qualified workers to oversee those contractors. HUD suffers from inadequate monitoring systems, and employs people with the wrong skills in the wrong place.

The HUD Office of Inspector General has come to similar conclusions. A 2000 comprehensive audit of FHA loan origination practices found significant problems with FHA's reviews of lender underwriting and property appraisals as well as deficiencies in the monitoring of lenders by HUD's Quality Assurance

Division. The OIG also reported problems with the oversight of pre-endorsement contractors, and the accuracy of information in the automated tracking system. These weaknesses increase HUD's risk and can result in inflated appraisals, fraudulent underwriting, property flipping, and other lending abuses.

Before HUD begins another complex program—the sanctioning of appraisers based on defaults—it should integrate its existing monitoring systems. As the GAO states, the current systems do not talk to one another. For example, to get information on a lender, one would have to utilize four different systems: one to access a lender's address, one to discover the value of loans it disburses, one to look at its default and claims rates and one to read any complaints filed against it.

Problem 9: Elimination of the latest appraisal systems appears not to have been justified

In its April 1999 report (*Single-Family Housing: Weaknesses in HUD's Oversight of the FHA Appraisal Process*) the GAO recommended to HUD the incorporation of a Real Estate Assessment Center (REAC). Under the HUD 2020 Management Reform Plan, HUD created REAC, which set out to design totally new systems based on a paperless, e-business model. In June 2000, REAC implemented the Appraisal Quality Assessment (AQA) process. The AQA process was designed to address the deficiencies in appraisal oversight outlined in the GAO April 1999 report.

This year, HUD officially cancelled the Appraisal Quality Assessment Services contract, which administered the Single Family Appraisal Subsystem of REAC. According to a special notice provided by HUD on March 13, 2002, "The Department has determined it is in the best interest of the government to cancel this solicitation."

In January 2000, three members of the Appraisal Institute were awarded the prestigious "Hammer Award" for their efforts with the Single Family Appraisal Subsystem of REAC. The award recognized the members for their efforts in streamlining government processes and FHA programs specifically.

We were surprised to see HUD eliminate this program and are now concerned to see it replaced with the Appraiser Watch Initiative. The Appraiser Watch Initiative appears to be an inferior appraisal review and sanctioning process compared to AQA. According to HUD's own internal documents which have been stored at the GAO, from June 2000 through December 2001, the AQA program screened 1,380,427 appraisals, flagged 89,939 as in-house risk factors, and audited 36,071 at the REAC headquarters.

The HUD AQA program appeared to be addressing many of the long-standing concerns about HUD's Single Family appraisal review program. With the high number of appraisals that were flagged and audited by AQA, we wonder why only 33 appraisers were removed from the FHA Appraiser Roster during the program's existence. It would appear much of HUD's problems in this area were a result of deficiencies in the HUD sanctioning process rather than the review functions of AQA.

The GAO has even noted the AQA improved the FHA appraisal review process. During oral testimony at a July 24, 2002, Senate hearing on HUD management challenges, GAO's Stanley Czerwinski maintained that since its inception, REAC had been responsible for a significant improvement over past reporting shortcomings, doing a fine job of submitting information to HUD's Secretary and Deputy Secretary on HUD's partnerships with public housing agencies, multifamily owners, resident groups, lenders and appraisers. Yet even though the establishment of the AQA was recommended by the GAO

and was successful in its monitoring the appraisal review process, AQA was discontinued. Czerwinski concluded his Senate testimony by urging Deputy Secretary Alphonso Jackson to look at what works and what doesn't, where tensions and stresses actually exist. In other words, the GAO was perplexed that HUD would eliminate a program that actually appeared to work. HUD needs to establish measurable, specific goals and a viable mission statement for all of its programs.

Problem 10: Appraiser Watch fails to curb appraisal problems before they occur

Many of HUD's appraisal-related problems could be avoided if the Department chose to adopt stronger mitigation efforts to ensure that qualified appraisers are performing appraisal assignments and that HUD employees are trained sufficiently to review the work of fee appraisers. Basing a system on a default rate, which often does not occur until years after the loan has been created, fails to improve the overall performance of the FHA Appraiser Roster or HUD management systems. Although we applaud HUD's efforts to remove appraisers with a bad performance record, we feel HUD should place more of an emphasis on solving problems before they have started.

Summary of Problems

Our respective organizations urge HUD to address the systemic problems in its appraisal programs and abandon the Appraiser Watch Initiative. For HUD to attract highly experienced and educated appraisers to be involved with FHA appraisal program, it must address the issues stated above.

Suggestions

In addition to the problems pointed out above, we hope HUD will consider the following suggestions if it proceeds to finalize the Appraiser Watch Initiative. These suggestions are outside the scope of the Appraiser Watch Initiative, yet we hear from our members that these issues should be addressed.

Suggestion 1: Review appraisers on the quality of appraisals

HUD should review appraisers by the quality of the appraisal. This offers the best way for HUD to review the quality of FHA appraisers.

Flagging potentially inaccurate appraisals is an area in which recent technology developments present cost-effective solutions. 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.

Automated monitoring systems that flag potentially fraudulent appraisals are becoming more and more common in the marketplace. HUD could benefit from such a mechanism that would identify faulty appraisals and aid in efficient sanctioning of appraisers perpetrating fraud or purposeful inaccuracies.

The Appraisal Institute and FNC, Inc. recently cosponsored a Congressional staff briefing providing information on FNC's Collateral Management System (CMS), which could be a possible solution for federal housing fraud problems. The CMS automates not only pre-funding review, but also the ordering and procurement of collateral services necessary to the mortgage loan origination process. The CMS uses a new technology standard called "AI Ready," developed by FNC and the Appraisal Institute that allows secure data communication across multiple platforms. AI Ready forms are consistent with the

Appraisal Institute's Residential Data Storage Standard. If implemented, the CMS would provide HUD the ability to automate appraisal review and fraud detection.

Suggestion 2: Enforce lender accountability for appraisals

Under Lender Select, FHA gave lenders responsibility for the quality of appraisals being performed. Yet the lender accountability provision of Mortgagee Letter 94-54 has never been enforced.

We suggest HUD actively enforce the provision on lender accountability over 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 over 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.

Suggestion 3: Establish policies on client pressure and provide information to appraisers

Mortgagee Letter 94-54 contains a section on "Pressure on Appraiser and Conflicts of Interest." This section states:

"The Department requires that appraisers chosen under this new procedure not be supervised or directed by any loan officers or loan production personnel. Chosen appraisers should be supervised by the lender's underwriting or management personnel. Instances of undue pressure or influence on an appraiser reported to HUD will result in appropriate disciplinary actions against the lender involved."

Although we are pleased HUD has accepted that undue pressure of appraisers exists, we feel the Department could do much more by providing more information to appraisers on the existence of HUD's requirements. Most appraisers are simply unaware that HUD will accept complaints against lenders applying undue pressure. Typically, they do not know whom to contact within the HUD bureaucracy, and no procedure has been established by HUD on how the appraiser is to submit his/her complaint.

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.

In addition, we are aware of instances where some realty agents attempt to influence lenders to direct FHA Appraisal Assignments to certain appraisers over others. Inappropriate pressure is sometimes applied to not use specific appraisers they believe will jeopardize their deal either with repairs required or values below the contract price. Just as the loan officer may attempt to influence the appraiser with a threat of no future business, these real estate agents, operating contrary to the Code of Ethics of the

NATIONAL ASSOCIATION OF REALTORS®, may attempt to similarly influence the lender or the appraiser. Note that not all real estate agents are subject to the NAR Code of Ethics.

Such influence has caused our members to raise concerns over the credibility of HUD's appraiser selection process. In fact, the 1999 Third Quarter Report of the HUD Office of Inspector General's Report stated concern over this issue:

"While HUD regulations require lenders to select and be responsible for the work of single family property appraisers, the regulations do not prohibit lenders from selecting appraisers recommended by real estate agents. However, in our opinion, lenders acquiescing to influence from real estate agents in the selection of appraisers calls into question the appraiser selection process. HUD requires lenders to exercise due diligence in choosing only the best-qualified and knowledgeable appraisers. However, HUD has little assurance that lenders are exercising due diligence in the selection of appraisers if lenders are being pressured to select certain appraisers."

The HUD OIG audit 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.

Suggestion 4: Review policies relating to financing and seller concessions

We suggest HUD revise its policy in relation to financing and seller concessions such as discount points, down payment assistance, settlement assistance, buydowns, etc. We believe that unless HUD holds appraisers accountable for ignoring seller concessions, HUD should require the buyer pay their own closing costs and not allow seller assistance or financing incentives.

Therefore, we support HUD issuing a letter to all approved appraisers on the FHA Appraiser Roster to help emphasize the importance of appraisers reporting, analyzing and adjusting for financing and seller concessions. Such a letter could state:

1. The appraiser must disclose when selling concessions exist on the subject as well as comparable sales;
2. Comparable sales used by the appraiser must be adjusted for selling concessions, discount points, settlement assistance, seller contributions, etc;
3. Failure to make adjustments will result in removal from the HUD Appraiser Roster and all reports with such violations will be sent to the state licensing board.

Suggestion 5: Remove unqualified appraisers from the FHA Appraiser Roster

On January 29, 2002, our respective organizations submitted comments to HUD regarding the Proposed Rule on Appraiser Qualifications for Placement on the FHA Single Family Appraiser Roster. This Rule was designed to strengthen the licensing and certification requirements for placement on the FHA Appraiser Roster. Among other things, the Proposed Rule requires that appraisers on the Appraiser

Roster have professional credentials that are based on the minimum licensing/certification standards issued by the Appraiser Qualifications Board (AQB) of The Appraisal Foundation. We reviewed the Proposed Rule and agreed that the proposed actions represent a sound first step in addressing problems related to the Appraiser Roster. However, even though HUD instituted similar requirements more than two years before the Proposed Rule was released, hundreds of unqualified appraisers were accepted on the FHA Appraiser Roster because of administrative loopholes. We have continually recommended HUD take immediate steps to remove them to maintain the integrity of the FHA Appraiser Roster.

We are discouraged that HUD still has not addressed this problem. HUD admitted there were hundreds of unqualified appraisers on the FHA Appraiser Roster, yet it set forth no procedure for removing them. In fact, under that proposed rule, no action was taken against the unqualified appraisers. HUD should address this problem and ensure that qualified appraisers are performing assignments for FHA.

Suggestion 6: Address high-volume appraisers

A development in Georgia has highlighted the problem of appraisers performing “extraordinarily high volumes” of FHA appraisals. Recently, a member of the Appraisal Institute alerted the HUD Inspector General to this problem. A common arrangement in these cases is for FHA-approved appraisers to have “trainees” (who are not approved for the FHA Appraiser Roster) perform interior inspections of homes and then for the FHA-approved appraiser to sign the reports as if they had inspected the homes themselves. According to recent information provided by HUD, many appraisers had performed in excess of 1,000 appraisals in a given year (almost 3 appraisals per day for 365 days), which appears to be a clear violation of HUD’s appraisal policies.

The HUD Atlanta Homeownership Center responded in March 2002, saying it was able to identify 10 appraisers who completed in excess of 500 appraisals in 2001. Of those 10 appraisers, two were removed from the FHA Appraiser Roster in 2001 for a period of one year. The Atlanta HOC also committed to monitor reviews of appraisals completed by the remaining eight active appraisers. However, under HUD’s Proposed Rule whereby appraisers would only be monitored according to a default rate, it is unlikely HUD would take any action against these appraisers. We recommend HUD institute policies immediately to ensure approved FHA appraisers research, inspect and complete FHA appraisal assignments appropriately.

In addition, according to HUD Valuation Handbook 4150.2, Section 7-3, HUD is required by law to refer appraisers to state appraiser boards if it feels a case warrants such a referral. There has been no indication that HUD has referred any of the individuals involved in these cases to the Georgia Real Estate Appraisers Board. In addition to addressing the problem of high-volume appraisers, we strongly encourage HUD to refer deserving cases to state appraiser boards for possible further action.

Suggestion 7: Increase FHA education/qualifications requirements and HUD staff training

HUD should strive to have the most qualified and experienced appraisers performing appraisals on its behalf. It should also ensure its headquarters and field staff are sufficiently trained in appraisal practices and methodologies to review the work of fee appraisers. We suggest the test for acceptance on the appraiser roster be modified to raise standards to ensure that highly qualified and experienced appraisers are accepted on the roster. 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 FHA Appraiser 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.

In addition, members of our organizations have demonstrated a high level of experience and competency in issues of concern to HUD. We would like to see HUD make an effort to recruit members of professional societies, as they represent the best possible source for appraisal work due to stringent continuing education requirements and adherence to the highest professional ethics and standards. Conversely, the qualifications and education of appraisers have remained constant or have been reduced. Meanwhile, defaults and mortgage problems have increased. Members of professional societies, if actively involved, represent a great resource to HUD that is currently being ignored.

HUD has made some positive steps in regards to training staff to ensure competency with appraisal issues. During July, August, and September of 2002, the Appraisal Institute presented real estate appraisal training courses at the Denver, Philadelphia, and Santa Ana Home Ownership Centers for the Office of Housing, Single Family Insured Housing Division of HUD. The courses presented met the education requirements of the Appraiser Qualifications Board of the Appraisal Foundation for appraisal licensing. The courses were taught by practicing appraisers with many years experience in the single-family market. The courses brought fresh perspectives to HUD employees and were well received. 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 the Office of Housing and should improve the operations of the Home Ownership Centers. We encourage HUD to embark these types of training projects on a more regular basis.

Concluding remarks

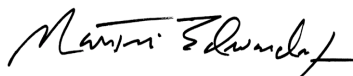
We appreciate the opportunity to comment on the Appraiser Watch Initiative. We hope these comments will be taken into consideration by HUD during the course of implementation of any new initiatives.

Should you have any questions, please contact Don Kelly, Vice President of Public Affairs, Appraisal Institute at 202-298-5583 or dkelly@appraisalinstitute.org, Ted Baker, Executive Vice President, American Society of Appraisers at 703-733-2019 or tbaker@appraisers.org, or Peter Morgan, Senior Regulatory and Industry Relations Liaison, National Association of Realtors at 202-383-1233 or pmorgan@realtors.org.

Sincerely,



Thomas A. Motta, MAI, SRA
President
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Martin Edwards, Jr., CCIM
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John Connolly, ASA
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