Office of Thrift Supervision
Department of the Treasury

Timothy T. Ward
Deputy Director, Examinations, Supervision, and Consumer Protection

1700 G Street, N.W., Washington, DC 20552 • (202) 906-5666

April 30, 2008

Home Valuation Code of Conduct Response
Attn: Senior Vice President, Credit Risk Oversight
Freddie Mac
1551 Park Run Drive, Mail Stop D2Z
McLean, VA 22102-3110

To Whom It May Concern:

The Office of Thrift Supervision (OTS) submits this comment letter regarding the Home Valuation Code of Conduct ("Code") and the Home Value Protection Program and Cooperation Agreements ("Agreements") entered into by the New York Attorney General, Fannie Mae, Freddie Mac, and the Office of Federal Housing Enterprise Oversight (OFHEO) (respectively, and collectively, the "Parties") on March 3, 2008. The OTS is interested in the Code and the Agreements given their potential for economic consequences on the federal housing and mortgage markets. In OTS's unique role as the federal regulator of savings associations and savings and loan holding companies, the OTS supervises an industry comprised primarily of mortgage lenders.

OTS regulated institutions are subject to appraisal standards of independence and minimum appraisal requirements, all of which are described in the OTS Appraisal Regulation at 12 C.F.R. Part 564. This regulation is consistent with the appraisal regulations adopted by the other federal banking agencies. The federal banking agencies have issued joint guidance to be read in conjunction with each agency's appraisal regulation.[1] Moreover, licensed appraisers are subject to industry standards such as the Uniform Standards of Professional Appraisal Practice (USPAP). USPAP is incorporated in the OTS Appraisal Regulation and constitutes a minimum appraisal requirement for our supervised institutions.

Our Appraisal Regulation and Interagency Guidance cause an appraisal program to be isolated from influence by loan production staff. Reporting lines for staff who order, accept, perform or review appraisals should be independent of loan production. Similarly, individuals who oversee the appraiser selection process must be independent of the loan production area.

The Code would preclude many federally regulated institutions from using in-house appraisers, as well as appraisers employed by certain affiliates or subsidiaries, to perform appraisals on transactions that are eligible for sale to Freddie Mac and Fannie Mae. OTS disagrees that corporate structure and ownership considerations alone would dictate whether an appraisal was prepared with proper independence.

Imposing a requirement that all lenders must outsource appraisals will not ensure appraiser independence and may make regulatory enforcement more difficult. As I noted earlier, sufficient laws, regulations, and

[1]Specifically, OTS has issued Thrift Bulletin 55a, Interagency Appraisal and Evaluation Guidelines, dated October 27, 1994, (http://www.ots.treas.gov/docs/8/84042.pdf), CEO Letter #184, Independent Appraisal and Evaluation Functions, dated October 27, 2003, (http://www.ots.treas.gov/docs/2/25184.pdf, and CEO Letter #213, Frequently Asked Questions (FAQ) on the Agencies' Appraisal Regulations and Related Guidance, dated March 22, 2005, (http://www.ots.treas.gov/docs/2/25213.pdf) (collectively "Interagency Guidance").

guidance exist to achieve the universal goal of appraisal independence, irrespective of whether the appraisal process is conducted in-house or through outside vendors.

The Code's provisions would require financial institutions to revise their internal operations, including related compliance functions and technology, to sell loans to Fannie Mae and Freddie Mac. Savings associations with in-house appraisers will likely incur significant internal operating costs to comply with the Code. These potential costs include: restructuring of internal operations; terminating existing contracts and business relationships; updating technology for the Code's provisions; testing for compliance; managing terms of new representations or warranties; and selecting new appraisal service providers.

Moreover, the Code as currently drafted could have a significant impact on savings associations utilizing subsidiary or affiliate companies engaged in the appraisal business. If unable to utilize qualified appraisers employed by these entities, savings associations could be forced to close or sell their ownership interest in subsidiary or affiliate companies engaging in appraisal or real estate settlement activities. The costs associated with such actions could be significant. As long as the independence of the appraisal process is ensured, there is no reason to prohibit such affiliations or subsidiary business arrangements.

Additionally, the Code raises several questions as to its enforceability. The Code does not define how Fannie Mae and Freddie Mac will enforce the provisions in the context of representations and warranties or under what standards Fannie Mae and Freddie Mac may "put back" loans to a savings association. For example, the provisions addressing "appraiser coercion" are quite broad. Absent any details around how these new provisions will be interpreted and applied by Fannie Mae and Freddie Mac, institutions could face enormous exposure to the extent, for example, that an appraiser's claims of coercion cause Fannie Mae and Freddie Mac to invoke representations and warranties resulting in loans being "put back" to a savings association. Accordingly, OTS believes that institutions that it regulates will not be able to fully identify, manage, and monitor their credit risk under the ambiguous terms of the Code and could force our institutions into an "unsafe or unsound operation".

If Fannie Mae and Freddie Mac, two of the largest purchasers of home mortgages in the United States, are truly serious about improving the appraisal process, we suggest they develop and adopt certification and qualification standards for appraisers performing appraisals of properties securing loans they purchase and incorporate testing and review procedures to ensure the adequacy and integrity of the appraisal process.

Although OTS and the other federal banking agencies were consulted about the Agreements and the Code by OFHEO, this occurred on an expedited basis immediately prior to the formal announcement of the Code and Agreements by the New York Attorney General. The consultations were initiated at a point when it did not appear to encourage any meaningful collaboration or changes based on industry practice and our long supervisory experience. The financial institutions OTS regulates did not have an opportunity to fully comment on how these documents may directly or indirectly affect them or to explain their possible consequences.

The Agreements and the Code, in OTS's view, are the products of a flawed process. The documents, which purport to address a problem that affects the entire mortgage lending industry, are the result of a process that did not appropriately or adequately identify the problems for which the Code is intended to rectify and/or alternative remedies to address any identified problems. The Code and the Agreements would effectuate sweeping changes in the industry and do not allow for a case-by-case approach. The documents were prepared without the benefit of appropriate industry or regulator input and do not take into account the actual and potential effects and consequences upon OTS-regulated lenders.

OTS recommends that the Parties carefully consider all comments received during this period and delay efforts to improve the appraisal process through implementation of the Code until the impact on regulated lenders can be more fully examined, explained, and understood. The Parties should not make any assumptions as to OTS's views on the provisions in the Code or Agreement that are not addressed in this letter, as we reserve the right to supplement this comment with future submissions, as deemed necessary.

Sincerely,

Timothy T. Ward
Deputy Director