Appraisal Institute®
Professionals Providing Real Estate Solutions

ASA

March 29, 2006

To: Office of the Comptroller of the Currency (Treasury) - Docket Number 05-21
Board of Governors of the Federal Reserve System - Docket Number OP–1246
Federal Deposit Insurance Corporation
Office of Thrift Supervision (Treasury) – Docket Number 2005–56
National Credit Union Administration

Re: Interagency Guidance on Nontraditional Mortgage Products

We are writing to express support for the December 29, 2005, **Interagency Guidance on Nontraditional Mortgage Products**. We believe these guidelines will help raise awareness concerning the risks associated with nontraditional loan products, and reemphasize the importance of proper collateral valuation and appraisal management practices.

We are particularly supportive of your directive to financial institutions that their underwriting standards comply with the agencies' real estate lending standards, appraisal regulations and associated guidelines. While nontraditional loan products can expose financial institutions to increased risk, properly performed appraisals by qualified professionals can help institutions account for those risks.

For years–and more so recently–our members have reported the loss of appraiser independence, when they are directed to provide predetermined opinions of value to help facilitate transactions. Failure to adhere to such requests from loan officers, mortgage brokers and others has resulted in honest and ethical appraisers being placed on exclusionary or "do-not-use" lists. Our organizations support and encourage increased scrutiny of third-party originators such as mortgage brokers and correspondents. As you have indicated, if third-party originator appraisal problems are discovered, the institution should take immediate action, which could include terminating its relationship with the third party. We encourage you to retain such language in your guidance and actively enforce this provision during bank examinations.

One concern that has remained unaddressed since the agencies promulgated the 1994 Final Rule on Real Estate Appraisals is the definition of "financial services institutions," such as mortgage lenders and mortgage brokers, and their ability to engage real estate appraisers. As this rule was being considered, appraisers and others warned that allowing financial institutions to order appraisals would lead to greater pressure applied on real estate appraisers. Yet the agencies retained the allowance in the Final Rule largely for regulatory relief measures. Twelve years after the Final Rule, our members routinely report that breakdowns in appraisal independence are more likely to occur when engaged by financial services institutions rather than regulated institutions.

Since the publication of the Final Rule, the mortgage lending and mortgage brokerage industries have evolved and become more defined. Most states now license or register mortgage lenders and mortgage brokers, and many of those that do not are currently considering such legislation. While we recognize that amending a regulation is no small feat, our organizations believe that further definition and scoping of the agencies' expectations of financial services institutions and their interaction with regulated institutions are in order and would promote safety and soundness.

Our organizations would also support the establishment of a specific review requirement where a stipulated percentage of loans or certain mortgage-risk classifications (LTVs above 90 percent, for instance) would be reviewed by qualified review appraisers. Through past interagency guidance, your agencies have recognized that a robust appraisal review function is an important element of an institution's policies and procedures. However, the lack of a specific requirement too often means that very few or no reviews are performed at all in some regulated institutions and financial services institutions. We recognize that this may be viewed as an additional expense to be undertaken by financial institutions, but we hope that this would be viewed more positively as a loss mitigation tool, and we would encourage its exploration.

Finally, we are also supportive of other provisions of the proposed guidance, including:

- Cautioning against "collateral-dependent mortgage loans" by reminding institutions that such loans are unsound and may be subject to criticism, corrective action and higher capital requirements.
- Highlighting the increased use of risk-layering practices (reduced documentation and/or simultaneous second-lien loans), which expose financial institutions to increase risk.
- Raising awareness about ceding underwriting standards to third parties that have different business objectives, risk tolerances and core competencies.
- Reminding institutions that portfolio and risk management practices should keep pace with the growth and changing risk profile of their nontraditional mortgage loan portfolios and that active portfolio management is especially important for institutions that project or have already experienced significant growth or concentrations of nontraditional products.

Our members are dedicated to assisting institutions wherever possible with their collateral management needs, stress testing on housing value fluctuations, regulatory compliance consulting and portfolio management issues. We support alerting institutions, particularly small institutions with limited resources, that such resources are available and can be obtained by contacting our organizations or performing a "find an appraiser" search on our websites.

Thank for you the opportunity to provide comment on this important issue, and we look forward to working with you following its implementation. Should you have any questions or need further information, please contact Don Kelly, Vice President of Public Affairs, Appraisal Institute, at 202-298-5583 or dkelly@appraisalinstitute.org.

Sincerely,

Appraisal Institute (www.appraisalinstitute.org)
American Society of Appraisers (www.appraisers.org)
American Society of Farm Managers and Rural Appraisers (www.asfmra.org)