Appraisal Institute
Professionals Providing Real Estate Solutions

American Society of Appraisers
ASA
The International Society of Professional Valuers

Property Economics Professionals
ASFMRA

NAIFA

July 30, 2009

Federal Trade Commission
Office of the Secretary
Room H-135 (Annex T)
600 Pennsylvania Avenue, NW
Washington, DC 20780

Re: Mortgage Acts and Practices Rulemaking, Rule No R911004

Dear Sir or Madam:

The undersigned professional appraisal organizations, representing 35,000 credentialed real estate appraisers in the U.S., appreciate the opportunity to comment on the Commission's Advanced Notice of Proposed Rulemaking (ANPR) involving "Mortgage Acts and Practices". The ANPR seeks comment on the types of mortgage-related acts and practices occurring throughout the life-cycle of a mortgage loan that should be prohibited or restricted because they meet the FTC's standards for unfairness or deception under Section 5 of the FTC Act. <u>Appraisals are specifically included</u> as an activity that occurs during the mortgage life-cycle[1]; and the ANPR seeks responses to a series of questions about whether and how an FTC rule, which prohibits or restricts appraisal-related acts and practices deemed unfair or deceptive to consumers, should be constructed. Our comments are limited to a discussion of issues relating to appraisals performed in connection with mortgage lending by financial entities within the Commission's regulatory jurisdiction.

---

[1] In addition to appraisals, the ANPR describes the mortgage life-cycle as including loan origination, marketing, advertising and servicing.

I. <u>Executive Summary</u>

- Determinations of the fair market value of residential property collateralizing mortgage loans are critically important to consumers because they greatly influence whether a lender will approve the consumer's loan application; <u>and,</u> because they are a major factor in the terms and conditions of the consumer-borrower's debt obligations. Accordingly, <u>acts or practices by a nonbank financial company that impede the reliability, objectivity or overall integrity of the fair market value determination, deprive consumers of information crucial to their decision-making about a home purchase and about the acceptability of financing arrangements</u>. For this reason, such acts or practices should be regarded as "unfair" (because they are likely to cause substantial economic injury to the consumer) and/or "deceptive" (because they are likely to mislead the consumer in a material way) in clear violation of Section 5 of the FTC Act;

- Our organizations respectfully urge the Commission to act with dispatch to promulgate proposed rules delineating the specific acts and practices by nonbank financial institutions likely to deprive consumers of crucial information about the fair market value of property to be mortgaged that they would have received from an independent and professional appraisal. In this regard, we share the conclusion of the Commission staff that while the federal banking agencies have established "appraisal guidance that applies to entities under their jurisdiction…there is no equivalent federal guidance for nonbank entities under the FTC's jurisdiction";

- In response to the ANPR's important questions about the effect on competition and consumers if the FTC's appraisal rules prohibit or restrict acts and practices of nonbank lenders more rigorously than the appraisal rules of the federal banking agencies, we offer the following:

  <u>First</u>, our organizations are convinced that <u>rigorous application of Section 5's provisions to acts and practices which undermine the integrity of the appraisal process, would be of enormous</u>

benefit to the millions of consumers whose mortgages are originated by nonbank entities; and, would greatly enhance competition for mortgage services between banks, thrifts and credit unions, on the one hand; and, nonbank lenders, on the other. We believe that the prospect of a consumer's receiving a well-documented appraisal report from an independent, professional appraiser when a mortgage is originated by a nonbank lender vs. the possibility that they will receive a superficial valuation product from some banks because the regulators allow it, will become a significant element of competition for mortgage services.

Second, we strongly reject the notion that in considering which nonbank lender acts or practices relating to appraisals are unfair or deceptive under Section 5, the Commission should be mindful in any positive way of the lax appraisal policies of the federal banking agencies. For a variety of valid reasons (including, the condition of the nation's mortgage lending markets; the Obama Administration's conclusion that the banking agencies' consumer protection responsibilities must be transferred to a new Consumer Financial Protection Agency; and, the thirteen categories of real estate-related financial transactions that the banking agencies have exempted from professional appraisal requirements), the banking agencies' appraisal policies have been judged by many to be seriously inadequate and should not serve as a model for the FTC;

- Our organizations believe that the following acts and practices relating to determining the fair market value of properties to be mortgaged, are contrary to the interests of consumers and violate Section 5's prohibitions against unfair and deceptive practices in or affecting commerce:

(1) Any act or practice by a nonbank mortgage lender which permits individuals who are not licensed or certified as appraisers by competent state authorities, to provide an opinion of the market value of a property for any purpose relating to a mortgage;

(2) Any act or practice by a nonbank mortgage lender which permits the use of unregulated and/or untested valuation products – such as broker price

opinions, automated valuation models and tax assessment valuations – to substitute for a professional appraisal to value a property for any mortgage-related purpose;

(3) Any act or practice by (a) a nonbank mortgage lender which permits an Appraisal Management Company (AMC) owned or retained for the purpose of providing it with the fair market values of properties collateralizing mortgage loans, to hire or manage appraisers in a way which violates the Competency, Ethics and other provisions of the Uniform Standards of Professional Appraisal Practice (USPAP); and, (b) by an Appraisal Management Company whose policies, practices or procedures are likely to cause the conduct of appraisers hired to perform appraisals, to violate USPAP provisions. We believe that many and perhaps most Appraisal Management Companies are within the FTC's authority to regulate the activities of firms which provide mortgage-related financial services (including appraisal services) not just to nonbank lenders but also to banks, thrifts and credit unions.

II. Background

The entities to be covered by proposed rulemaking are those over which the Commission has jurisdiction under the FTC Act – specifically, firms that engage in mortgage-related acts and practices but which are not regulated by the federal banking agencies. These mortgage origination entities, which number in the thousands and account for billions of dollars in subprime and prime mortgage loans, are referred to in the ANPR as "nonbank financial companies".[2] While the FTC Act specifically excludes banks, thrifts and federal credit unions from the agency's enforcement jurisdiction, affiliates and subsidiaries of these federally regulated financial institutions, which are not banks themselves, are subject to the Commission's jurisdiction. Also subject to FTC jurisdiction are entities which provide "financial services" to such institutions under contract arrangements.[3]

[2] Although the precise number of non-depository mortgage lenders is not known, they are believed to make hundreds of billions of dollars of mortgage loans (including more than half of all subprime mortgage loans) and employ hundreds of thousands of individuals.

[3] The federal banking agencies recently added appraisal services to their definition of "financial services" .

FTC jurisdiction over (a) nonbank mortgage lenders who rely on appraisals to establish the market value of residential properties collateralizing their loans and (b) firms which provide mortgage-related financial services – including appraisal services – to banks, thrifts and credit unions (either as their affiliates or subsidiaries or as contractors) is obviously of great importance to our organizations.

Section 5 of the FTC Act broadly prohibits deceptive or unfair acts or practices in or affecting commerce. According to the ANPR, "an act or practice is <u>deceptive</u> if there is a [material] representation, omission of information or practice that is likely to mislead consumers who are acting reasonably." An act or practice is regarded as <u>unfair</u> if it causes or is likely to cause substantial injury to consumers so long as the injury is not outweighed by countervailing benefits to consumers or to competition. Finally, the injury must be one that consumers could not reasonably have avoided. Thus, "the Commission considers whether the harm is offset by any countervailing benefits to consumers or to competition…. In applying its unfairness standard, the Commission takes the approach that well-informed consumers are capable of making choices for themselves. Acts and practices can be prohibited or restricted if there is an "obstacle to the ability of consumers to make informed choices."

Why The FTC's ANPR Is Important To Our Professional Appraisal Organizations and To the Entire Community of Real Estate Appraisers

The Advanced Notice of Proposed Rulemaking is extremely important to our organizations and to the approximately 100,000 state licensed or certified real estate appraisers in the U.S. who provide valuation services in connection with mortgage lending or refinancing. Fair market value appraisals performed in connection with the purchase and financing of 1–4 family residential properties are of vital importance both to the consumer/homebuyer and to the mortgage lender. Appraisals are important to consumers because they provide them with an independent, objective and competent opinion of the value of the property they are seeking to purchase and finance;[4] and, they provide lenders underwriting mortgage loans a reliable understanding of the value of the property serving as collateral for repayment of monies provided borrowers.

Evidence of the central importance of appraisal services to mortgage-related acts and practices of the kind being reviewed by the FTC, can be found in the panoply of rules, regulations and policies governing the appraisal process by a variety of federal agencies responsible for administering programs whose success is dependent, to a significant extent, on reliable opinions of the fair market values of various types of property. For example, the Internal Revenue Service has recently issued interim rules and is close to issuing final rules, on the qualifications necessary to perform tax-related appraisals and the uniform manner in which they should be performed. But, the most obvious example of the importance of appraisals (and the one most immediately relevant to the subject matter of the ANPR), relate to the fact that the federal banking agencies have established appraisal policies in connection with the safety and soundness of real estate lending activities by federally insured and regulated depository institutions. The existence of the banking agencies' appraisal rules and policies were mandated in 1989 (Title XI of the Financial Institutions Reform, Recovery and Enforcement Act or FIRREA) by a Congress deeply concerned over the collapse of the S&L industry in the mid-1980s, including the absence of meaningful federal standards for the performance of real estate appraisals on properties collateralizing hundreds of billions of dollars in loans. Among other things, Title XI required states to certify or license individuals performing appraisals for many federal purposes and it mandated that all such appraisals comply with the Uniform Standards of Professional Appraisal Practice (USPAP). Although the banking agencies – at the behest of the depository institutions they regulate – wrongly utilized their administrative discretion to exempt large numbers of real estate-related financial transactions from Title XI's strong appraisal requirements, subsequent decisions recently made by Fannie Mae and Freddie Mac plugged many of the banking agency-created loopholes in connection with housing loans purchased by the GSEs for resale as securities in the secondary mortgage markets.

---

[4] All parties to the sale and financing of a residential property – except for the appraiser – have a stake in the "deal getting done". If the sale is not consummated, the real estate agent or broker doesn't receive his or her commission. If the financing is not approved, the mortgage broker and the mortgage lender don't receive their payments. By contrast, the appraiser works on a fixed-fee basis and gets paid whether or not the mortgage financing is approved. Moreover, only the appraiser is required, by enforceable ethical standards, to be a disinterested and objective party to the transaction.

Final FTC rules establishing impermissible appraisal-related acts and practices by thousands of nonbank lenders will fill a serious void and greatly benefit millions of consumers whose loans are made by these entities. Our organizations hope and trust that the Commission's rules will do for consumer protection what the appraisal policies established by the federal bank regulatory agencies in this area, have completely failed to do – protect consumers from abusive and sharp practices. Indeed, the Commission is in a position, through its rulemaking, to set an appropriately high standard of consumer protection relative to the mortgage finance process that could serve as a model for the banking agencies.

III. Recommendations Regarding Acts And Practices Involving Mortgage-Related Appraisal Services That Should Be Considered Unfair Or Deceptive To Consumers Under Section 5 of the FTC Act

The Commission's Advance Notice of Proposed Rulemaking asks for public and stakeholder comments in response to a series of detailed questions involving appraisals performed for mortgage purposes. While each question posed in the ANPR section entitled "Mortgage Appraisals" is thoughtful and deserves a thoughtful response, our organizations believe that the most important question by far that is asked (it is asked several times) involves the potential effect "on competition and consumers…if the Commission were to prohibit or restrict nonbank financial companies with respect to [appraisal-related] acts or practices, but banks, thrifts and federal credit unions were not similarly prohibited or restricted?" We appreciate the opportunity to take on that question and its public policy implications. Our response is as follows:

For a variety of reasons we believe persuasive, our organizations strongly believe that the FTC should adopt mortgage-related policies which are fully faithful to its consumer protection mission, irrespective of the approach taken by the bank regulatory agencies to similar issues. To do otherwise would be tantamount to willingly participating in a race to the bottom of the regulatory heap. Entirely apart from our organizations' critical views of the mortgage-related appraisal policies of the banking agencies, we believe it is appropriate and necessary for the Commission to consider the contribution of those policies to the current crisis in today's housing and mortgage markets. We also believe it is appropriate for the Commission to take note of the fact that the Obama Administration has determined that the banking agencies have done an inadequate job of protecting consumers in regulated financial transactions and is asking Congress to transfer those responsibilities to a new consumer financial protection agency. Accordingly, we see no merit whatsoever in using the appraisal policies of the federal banking agencies as a useful template against which to measure the public policy adequacy or effectiveness of the FTC's policies in this area. We hope the Commission agrees.

Consider, as well, the implications of a government agency's refusal to adopt public policies dictated by its statutory responsibilities and justified by conditions in the marketplace merely because those policies would impose consumer protection requirements that are substantially more rigorous than those established by other regulatory agencies. It is also relevant to recognize the distinction in the central focus of the FTC as opposed to that of the banking agencies. The principal focus of the Commission is to protect consumers from unfair and deceptive acts and practices, while the primary focus of the federal banking agencies is to ensure safe and sound loan underwriting by federally insured financial institutions. While these two missions should be complementary and compatible for the most part, the fact remains, in our view, that consumer protection has not been an important focus of the banking agencies.

Finally, we firmly believe that the Commission's adoption of rules determining that certain acts and practices relating to appraisals violate Section 5 of the FTC Act, will not only benefit millions of consumers over the years whose residential mortgage loans are underwritten by nonbank financial companies; but will also enhance competition for mortgage lending services between banks, thrifts and credit unions, on the one hand, and nonbank lenders, on the other. We believe that financial institutions which provide consumers seeking a mortgage with comprehensive and objective appraisal reports prepared by professional appraisers, will enjoy a competitive advantage over those mortgage lenders which do not.

With respect to the other mortgage appraisal questions asked in the ANPR, our organizations respectfully urge the FTC –

1. To adopt rules on unfair and deceptive acts and practices involving mortgage lending by nonbank financial institutions which specifically include appraisal services as a covered activity. Given the importance of independent and reliable appraisals of a property's fair market value to the terms and conditions of the mortgage loan and to the consumer/borrower's debt obligations, rules establishing unfair or deceptive acts or practices relating to the appraisal process should address the qualifications, independence and accountability of individuals providing fair market value opinions; and, should address as well, whether opinions of value have been developed in adherence to generally accepted appraisal standards of practice and ethics (specifically, the Uniform Standards of Professional Appraisal Practice or USPAP, recognized by Congress in Title XI of FIRREA);

2. To establish as an unfair or deceptive act or practice and incorporate into a proposed rule –

    - Any activity, decision or policy of a nonbank mortgage lender in connection with a mortgage origination, refinancing or modification, which permits the use of (a) unregulated and untested valuation products, such as broker price opinions, automated valuation models and tax assessment valuations or (b) individuals who are not state licensed or certified appraisers to determine the fair market value of collateral property.

    We strongly believe that reliance on untested and unregulated valuation products or on unqualified individuals to establish the fair market value of collateral property in connection with a consumer's mortgage loan meets the "deceptive" test of section 5 of the FTC Act because such practices are "likely to mislead consumers" on the actual value of their collateral property. We also believe that such practices are "unfair" under Section 5 in that they are likely to be unreliable and result, therefore, in substantial economic injury to consumer/borrowers. In this regard, it is important to note that consumer-borrowers are denied an opportunity to choose the method of valuation that will most likely produce an accurate market valuation of their mortgaged property – that is, an appraisal performed by a professional appraiser.

- Any activity, decision or policy of a nonbank mortgage lender permitting or enabling an Appraisal Management Company (AMC) owned or retained for the purpose of providing it with the fair market values of properties collateralizing mortgage loans, to hire or manage appraisers in a way which violates the Competency, Ethics and other provisions of the Uniform Standards of Professional Appraisal Practice; and, any activity or policy of an Appraisal Management Company which is likely to cause the conduct of the appraisers they hire to violate the provisions of USPAP.

The rapid growth of mortgage lender reliance on AMCs to provide appraisals in connection with loans has brought with it, widespread evidence that these vendors too often retain appraisers who live outside of and are unfamiliar with market conditions in the locality where the appraisal is to be performed – a likely violation of the Uniform Standards of Professional Appraisal Practice (USPAP); and, that they frequently require completion of appraisal assignments in unreasonably short time-frames – another potential USPAP violation. There is evidence that both practices often lead to poor quality appraisals.

We believe that the practice of hiring appraisers from outside the geographic area where the property to be appraised is located and not allowing them sufficient time to familiarize themselves with local markets; and, the practice of forcing appraisers to complete appraisal reports without sufficient time to perform a competent appraisal, both constitute unfair and deceptive practices under Section 5;

- Any activity, decision or policy of a nonbank mortgage lender which results in denying to borrowers a USPAP-compliant appraisal report on the fair market value of the financed property. When alternative valuation products are used to value a property (e.g., BPOs, AVMs or tax assessment valuations) the consumer is likely to receive a document that is of little or no use in understanding the basis on which the fair market value was reached. Our organizations believe that because BPOs and AVMs are not prepared in accordance with generally accepted standards; and because these valuation products and the individuals who prepare them are not subject to government regulation, these activities constitute an unfair and deceptive practice under Section 5.

IV. <u>Conclusion</u>

The FTC has a vital – and long overdue – role to play in assuring the millions of consumers whose loans are underwritten by nonbank lenders, that the fair market value of property they seek to finance has been determined independently and competently by valuation professionals; and that because of the reliability and comprehensive nature of that information, their ability to make mortgage-related decisions will be greatly enhanced. We hope the Commission finds our comments useful and favorably considers our recommendations.

Our organizations stand ready to meet with Commission members or staff to further explain our views. If you have any questions or wish to discuss these comments, please contact the government relations representative of the American Society of Appraisers in Washington, D.C., (Peter Barash, 202-466-2221, peter@barashassociates.com) or the government relations representative of the Appraisal Institute in D.C. (Bill Garber 202-298-5586, bgarber@appraisalinstitute.org.

Sincerely,

American Society of Appraisers
Appraisal Institute
American Society of Farm Managers and Rural Appraisers
National Association of Independent Fee Appraisers