NATIONAL ASSOCIATION OF APPRAISERS
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The Association for All Appraisers

September 30, 2011

Mr. Raj Date
Consumer Financial Protection Bureau
US Department of the Treasury
1500 Pennsylvania Avenue Suite 1801L
Washington, DC 20220

Re: Mortgage Loan Fees

The CFPB has provided two prototype forms for informing prospective borrowers of approximate funds needed to settle a mortgage loan origination. The NAA has reviewed both forms and applauds the simplification and uniformity exhibited. In fact, NAA has great confidence in the positive force the CFPB will be for both consumers of mortgage loans and for real property appraisers. It is in the interests of both groups that we wish to bring an important issue to your attention.

For appraising, both of the prototype forms list simply "appraisal fee," but do not clarify what this entails. Some lenders have developed a position that this is not the fee charged by the appraiser, but the fee the lender sets on the buyer that is intended to cover both the appraiser's fee and a fee for appraisal management. Appraisals are a "professional service," while appraisal management is an "administrative service." As may be seen in the enclosed summary, both VA and FHA underwrite their own appraisal management. Even so, large lenders often charge FHA borrowers an appraisal management fee by including it within the appraisal fee listed on the CFPB forms. The "appraisal fee" is listed as a fee for which the borrower-consumer may not shop. Traditionally, the cost of appraisal management has been considered to be a responsibility the lender to be paid out of the lender's origination fee. Most, if not all, other administrative services are covered within the origination fee. The new practice is almost exclusively that of large lenders, as local lenders, such as community banks and credit unions, still bear the management expenses out of their origination fee.

Dodd-Frank mandated that appraisers be paid "reasonable and customary" fees. There were two reasons for such a mandate. The first being that international investors in US mortgage instruments must have faith in the appraisals of the underlying collateral in mortgage loans. This faith has been seriously weakened, often as result of lender and AMC pressure to "push" values, to complete assignments in an unreasonably short time period and to accept discounted fees under the threat of denying future assignments. Consequently, appraiser independence is a critical aspect of Dodd-Frank, and an issue which will require CFPB attention.

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The second reason why appraisers must be paid a reasonable compensation is the fact that the borrower/consumer has a direct and major interest in the valuation since a home is probably the biggest purchase of their lives. In both these two cases it is necessary that the mortgage loan transaction be supported by an appraisal conducted by an appraiser who is competent for the specific assignment and who is paid sufficient compensation to permit a scope of work that meets the needs of both of the consumer and the ultimate investor.

As a result of the Dodd-Frank's reasonable and customary fee mandate, some large lenders have begun charging consumers even higher "appraisal fees," which they typically pass on to the appraisal management company to share with the appraiser, thereby forcing the borrower to pay more for appraisal management and the appraisal to the benefit of the lender, but to the detriment of both the consumer and the appraiser.

Inasmuch as these large lenders continue to resist underwriting the appraisal management expense, it is respectfully requested that the CFPB act to clarify that "appraisal fee," as stated on the forms represents the actual professional fee charged by the appraiser.

Your attention and service are sincerely appreciated,

George R. Harrison, PhD, MAA
President
GH/2
Enclosure: "Summary of Residential Appraisal History"

For additional current information on the issue:

1. Testimony of Sara W. Stephens, MAI, CRE to the House Committee on Financial Services; Subcommittee on Insurance, Housing and Community Opportunity, July 13, 2011
Mortgage Origination: The Impact of Recent Changes on Homeowners and Businesses

2. General Accountability Report to Congress, GAO-11-863, July 2011
Residential Appraisal -
Opportunities to Enhance Oversight of an Evolving Industry
(Both documents can be downloaded at www.naappraisers.org)

Cf:
Honorable Judy Biggert, Chair
Subcommittee on Insurance, Housing and Community Opportunities
House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Mr. David Vladik, Director
Bureau of Consumer Protection
Federal Trade Commission
600 Pennsylvania Avenue, NW
Washington, DC 20580

Summary of Residential Appraisal History from
The Mortgage Loan System, No. 015
The Columbia Institute, 2011

During the Great Depression the inventory of foreclosed homes throughout the country became overwhelming for the Building and Loan/Savings and Loan (S&L) industry. In 1934, in an effort to reduce this inventory, Congress created the Federal Housing Administration (FHA) to provide for lower down payments and lower monthly payments. The latter was to be accomplished through extended amortization. To implement this program the S&L only needed to take the loan application and complete certain FHA documents; and submit the documents to the FHA. If the borrower and collateral met FHA requirements, the FHA would issue a mortgage insurance document protecting the S&L from loss.

Unfortunately, S&Ls did not respond to this program and it was deemed a failure. In 1938 Congress attempted to salvage it by creating the Federal National Mortgage Association (FNMA; later to be known as Fannie Mae). FNMA was a US agency which would purchase FHA-insured mortgages with proceeds from the issuance of agency bonds. This resulted in the creation of the mortgage banking industry in the US and supported the great post-war housing boom. FNMA also became the source of financing VA loans when the VA was created in 1944. During that time S&Ls were essentially the only source of conventional loans, and mortgage banks were the source of FHA/VA loan services. Conventional loans by S&Ls were a small percentage of the housing market because of a limited source of funds. S&Ls had to rely on local community deposits, while mortgage banking companies could operate virtually anywhere in the country, having an open source of FHA/VA funds from FNMA. At this time, both mortgage banks and S&Ls were local institutions. The S&L used either staff or contract appraisers from a relatively small pool of local appraisers. Mortgage companies had no concern about appraisals since the appraisals were done by FHA/VA panels of fee appraisers. The appraisal fee was set by FHA or VA and was paid by the borrower to the lender who passed it on to the agency.

In the case of both the S&L and FHA/VA the borrower was charged an appraisal fee. The S&L fee for appraisals was set in agreement with the individual appraiser and any costs of appraisal management were borne by the S&L out of its fees. In the case of FHA and VA the appraisal fee was set by the agency and the management was borne by the agency. This remains the case today with VA. FNMA was privatized in 1968 so that it could purchase conventional loans in addition to VA/FHA. At that time FNMA created an appraiser approval program, but this was dropped in 1981. Congress also created a Government National Mortgage Association (Ginnie Mae) to buy FHA and VA mortgage loans, and it is the principal purchaser of such loans today, while Fannie Mae and its younger, smaller sibling Freddie Mac purchase essentially only conventional loans.

FHA eliminated its local panels in the early 1990s when it transferred appraiser selection and management to the lender. This was part of its "direct endorsement program." In the case of appraisal management, however, the program was ultimately

considered to be unacceptable, and in 1999 FHA returned to in-house appraisal management.

Under the FHA program, which remains in effect, FHA maintains a national roster of approved appraisers. The lender must choose an appraiser from this roster. In addition, FHA grades appraisers and sanctions those whom it finds to have committed infractions of standards or FHA requirements. Oddly enough, in either conventional or FHA assignment today a lender may contract with an appraisal management company (AMC), and pass the "appraisal fee" to the AMC. The AMC must then underwrite its both its management activities and that of the appraiser out of the "appraisal fee." In this scenario the assignment becomes what appraisers refer to as not being a "full-fee" assignment. In such cases, the AMC is clearly pushed toward the actual appraisal fee being the minimum obtainable as opposed to competency of the appraiser and credibility of the report.

Even when an AMC is used, however, the FHA is still the primary source of appraisal management. The FHA's approval of appraisers, its monitoring and reviewing of reports; and its sanctioning of appraisers is true appraisal management. This FHA activity is underwritten by FHA, even though the (large) lender requires the consumer to pay for both appraisals and appraisal management in one "appraisal fee." The small, local mortgage banks, community banks, and credit unions continue to accept that the appraisal management expense is their responsibility within the origination fee.

The use of AMCs is a new phenomenon in mortgage lending. It came about during the 1980s as mortgage lending shifted from exclusively local mortgage lenders to large national or regional lenders. Lenders' Services Incorporated (LSI) was probably the first AMC. It was established by Prudential Insurance Company primarily simply to locate appraisers in specific parts of the US wherever and whenever needed. Today, many claim that a major function of the AMC is appraisal quality control, and that may be true, but in the beginning it was simply to locate and communicate with appraisers. This is very clear in the case of LSI, since in 1992 it had only two certified appraisers on staff, but almost fifty clerical personnel to locate and communicate with appraisers. Today's AMCs do purport to provide quality assurance, although this continues to be the lender's responsibility. Consequently, the lender is obligated to provide its own internal review and quality control procedures. FHA's appraisal management program clearly demonstrates that it does not have confidence in appraisal management by either lenders or AMCs. Both Fannie Mae and Freddie Mac, however, have exercised little appraisal management as compared to FHA/VA and have experienced significant problems, but do attempt to hold lenders and/or mortgage insurers liable.

In addition to the FHA and VA having their own appraisal management programs, local lenders such as local mortgage banks, credit unions and community banks have their own management programs underwritten out of their origination fee, not by the borrower. In fact, the idea of the appraisal fee covering the cost of both the appraisal and appraisal management, is one of many phenomena of the entrance of big, national mortgage lenders replacing the pre-1990 localized mortgage lenders.