HPC
HOUSING POLICY COUNCIL

1750 K STREET, NW
SUITE 300
WASHINGTON, D.C. 20006
Tel. 202.589.1923

February 5, 2019

Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW.
Washington, DC 20551

Robert E. Feldman
Executive Secretary
Attention: Legal/ESS
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street, SW., Suite 3E-218
Washington, DC 20219

Re: Real Estate Appraisals; Docket No. R-1639; RIN 7100-AF30; RIN 3065-AE87; Docket ID OCC-2018-0038

Ladies and Gentlemen:

The Housing Policy Council[1] appreciates the opportunity to comment on the proposed rule to increase the threshold exemption for residential real estate-related transactions, the modification to the appraisal rule ("Proposed Rule") issued by the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (collectively, the "Agencies"). As discussed in more detail, HPC: (1) supports an increase of the threshold; (2) asks the Agencies to revisit and revise the guidance governing evaluations, which lenders must obtain for exempted transactions in lieu of appraisals; and (3) requests the Agencies promulgate the rule regarding quality control standards for automated valuation models ("AVMs") required by the Dodd-Frank Act.

1. **HPC Supports a Threshold Increase to $500,000.**

HPC supports the Agencies' decision to revisit the exemption threshold level for residential real estate-related transactions. As the Agencies correctly note, the threshold level has not been adjusted since 1994 and thus has not kept pace with home price appreciation. An increase in this threshold is long overdue. We request that the Agencies increase the

[1] The Housing Policy Council (HPC) is a trade association comprised of leading national mortgage lenders, servicers, mortgage insurers, and title and data companies. HPC advocates for the mortgage and housing marketplace interests of its members in legislative, regulatory, and judicial forums. Our interest is in the safety and soundness of the housing finance system, the equitable and consistent regulatory treatment of all market participants, and the promotion of lending practices that create sustainable home ownership opportunities leading to long-term wealth-building and community-building for families.

threshold from the current $250,000 to $500,000, rather than the proposed amount of $400,000.

Based on the indices the Agencies use in the Proposed Rule, an increase in the threshold to $500,000 would still reflect a conservative reading of the data and an appropriate level for the exemption. While the Agencies proposal focuses on housing prices in 2011, the more recent home price data shows a fairly significant differential that should be bridged with a higher threshold. A conservative approach that would not invoke safety and soundness concerns would be to set the threshold at $500,000. This value is still significantly lower than the 2018 value according to two of the three indices, and it is roughly the halfway point between the 2011 and 2018 data points for those two indices (Case-Shiller and FHFA).

Table 1 year	**Case-Shiller**	**FHFA**	**CPI**
1994	250,000	250,000	250,000
2006	578,813	511,636	341,109
2011	445,152	414,629	379,997
2018	641,191	611,700	424,031

This would be similar to the Agencies' approach in establishing the threshold for the commercial real estate ("CRE") exemption. The Agencies proposed a CRE threshold increase from $250,000 to $400,000, based in part on the CRE Index value at the lowest point in the most recent downturn, which was $423,000 in March 2010. However, in finalizing the CRE threshold, the Agencies raised the threshold to $500,000. Part of the Agencies' rationale, in addition to a safety and soundness analysis, was reliance on a more recent point in time for the CRE Index, finding that a $250,000 CRE loan in 1994 would be expected to have a conservative value of approximately $509,000 as of December 2017. Similar to the Agencies' reasoning for the CRE threshold, we ask the Agencies to use more recent data from residential real estate indices. Using that data, a $500,000 threshold for residential real property is appropriate.

Raising the threshold for residential real estate-related transactions to $500,000 would not pose additional risk to financial institutions because loans at or below this threshold will still be subject to an evaluation, which must be consistent with safe and sound banking practices. Valuation tools and models, such as AVMs, for residential real estate have improved significantly over the last decade, due to the extensive set of property data available. In fact, the rapid pace of sales in residential real estate has made evaluations extremely effective for some segments of the market. Of note, valuation models for properties between $400,000 and $500,000 are particularly accurate and predictive. Therefore, an adjustment in the threshold to $500,000 would not impose any risk to safety and soundness.

To ensure the threshold keeps pace for future home prices, we suggest that the Agencies schedule periodic adjustments to the threshold based on an inflation or housing price index, such as the indices the Agencies used in the Proposed Rule or the FHA or conforming loan limits. Alternatively, the Agencies could commit to a routine schedule for adjustments, based on a more manual review of housing price changes over some period of time, perhaps every five years. A more regular, scheduled adjustment, automated or manual, would be permitted under the Agencies' existing authority.

2. **The Agencies should provide enhanced guidance regarding evaluations.**

While a residential real estate-related transaction of $500,000 or less would be exempt from the appraisal requirements, financial institutions would still be required to conduct an evaluation in connection with the transaction.[2] Further, there are other types of transactions that are explicitly cited in the regulation that are also exempt from the appraisal requirement but subject to a property evaluation.[3] The Interagency Appraisal and Evaluation Guidelines ("Guidelines") set forth a set of parameters for institutions to conduct these evaluations. Since the Proposed Rule expands the number of loans subject to the evaluation requirement – an additional 214,000 originations (a number that would increase with the adoption of HPC's suggested threshold of $500,000), HPC believes that it is appropriate for the Agencies to reevaluate and revise the Guidelines regarding evaluations.

Specifically, we ask the Agencies to expand the evaluation component of the Guidelines to describe a range of permissible evaluation methodologies that take into consideration the substantial innovation that has occurred in the valuation industry, with new data sets and enhanced tools available to vendors and lenders alike. The use of data and technology enables new approaches to valuation that are entirely consistent with safe and sound banking practices. We expect the pace of change and innovation will continue in the coming years. More explicit permission for the use of automated alternatives to be acceptable evaluation methodologies would benefit all parties – borrowers looking for efficiency, lenders pursuing more effective digital strategies, and regulators seeking the impartiality and powerful analytics that are driving more accurate valuation methodologies nationwide.

Expansion of the Guidelines to address and allow these alternatives would also create an opportunity for a more uniform interpretation and application of the rules by examiners, providing clarity and confidence to all industry participants. In contrast, under the current Guidelines, HPC members have found that there are a variety of interpretations by examiners within and across the Agencies on what is considered an acceptable evaluation. This lack of consistency has caused confusion and hindered both the use of evaluations and the adoption of innovation in the market.

[2] 12 C.F.R. § 332.3(b).

[3] Specifically: the transaction involves an existing extension of credit at the lending institution, provided that: (i) there has been no obvious and material change in market conditions or physical aspects of the property that threatens the adequacy of the institution's real estate collateral protection after the transaction, even with the advancement of new monies; or (ii) there is no advancement of new monies, other than funds necessary to cover reasonable closing costs. There are additional categories of exempt loans that require evaluations, but HPC's focus is on residential real estate transactions.

The Guidelines should enable a Continuum of Alternatives.

The Agencies last revised the Guidelines in 2010, and since that time there have been significant innovation and developments in valuation methodologies, tools, data sets, all of which have improved the capacity of the industry to properly evaluate the condition, marketability, and value of properties. The combination of data, analytics, and technology developments warrant a revision of the approach to evaluations. We urge the Agencies to adopt a risk-based framework under which a range of evaluations methods may be utilized.

Under the current Guidelines, the Agencies instruct institutions to establish policies and procedures for determining when to obtain an appraisal, even though an evaluation would be permissible under the Appraisal Rule. As an example, the Agencies state that an institution should consider obtaining an appraisal as an institution’s portfolio risk increases or for higher risk transactions such as those involving: loans with combined loan-to-value (“LTV”) ratios in excess of the supervisory LTV limits; atypical properties; properties outside the institution’s traditional lending market; transactions involving existing extensions of credit with significant risk to the institution; or borrowers with high risk characteristics.

The Agencies should expand upon this risk-based approach to provide a continuum of evaluation options for lower-risk transactions. For the lowest risk transactions, an AVM would be appropriate. For the highest risk transactions, an interior/exterior appraisal would be required. The types of evaluations for moderate risk transactions could include a combination of models and techniques, such as an AVM with an interior inspection or an AVM with imagery for the probable condition. For transactions with moderate risk, the Agencies should establish risk-based factors to determine the type of evaluation that is appropriate and consistent with safe and sound banking practices. The Guidelines should explicitly permit a range of evaluation options based on the level of risk of the transaction, as evidenced by the full set of variables used in the loan underwriting.

To be clear, the risk factors would relate to all of three aspects of underwriting - borrower, loan, and property characteristics. Regarding the property itself, exemplary risk variables might include the date of the last appraisal, the level of sales activity in the community, whether the area has been affected by a natural disaster, as well as factors related to the transactions – for example, the LTV ratio, whether the property will be used as a primary residence. In addition, the risk factors must address the borrower profile, including the credit score, debt-to-income ratio, reserves available, and overall capacity and willingness to repay. Finally, the risk factors should consider other aspects of the transaction type, purchase or refinance, and the terms and conditions of that type of mortgage.

Most importantly, the continuum framework for evaluations should embrace the innovations and improvements in valuation methodology that have resulted from better use of data and analytics.

3. The Agencies should initiate the AVM rulemaking required under the Dodd-Frank Act.

We ask the Agencies to engage in the rulemaking mandated by the Dodd-Frank Act regarding AVMs. The Dodd-Frank Act amended FIRREA to establish parameters regarding AVMs. In particular, AVMs must adhere to quality control standards designed to: ensure a high level of confidence in the estimates produced by AVMs, protect against the manipulation of data, seek to avoid conflicts of interest, require random sample testing and reviews, and account for any other such factor the Agencies deem appropriate. The Agencies must promulgate a rule to implement these quality control standards.

There is increasing evidence that AVMs are effective, efficient, and, at many times, more predictive than standard appraisals.[4] With the appropriate quality control standards and with the consideration of risk-based factors, AVMs can be used to effectively evaluate a property's value in a manner consistent with safe and sound banking practices. The Agencies should consider an appropriate, risk-based exemption under the Appraisal Rule in which lenders may rely on AVMs without threatening safety and soundness. We would welcome a discussion with you on this AVM-only approach, should you be interested, prior to promulgation of the AVM rule.

In summary, we urge the Agencies to adopt a threshold exemption of $500,000. We ask the Agencies to provide an opportunity for comment on revisions to the Guidelines to adopt a more extensive risk-based approach that accounts for innovation and advancements. We also ask the Agencies to engage in the AVM rulemaking to further this risk-based approach. We look forward to working with the Agencies on these critical matters. Should you have any questions or need additional information, please contact Meg Burns our SVP for Mortgage Policy at 202-589-1926. Thank you for the opportunity to comment on the Proposed Rule.

Yours truly,

Edward J. DeMarco

Edward J. DeMarco
President
Housing Policy Council

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[4] *See, e.g.*, Federal Reserve Bank of Philadelphia, *Appraising Home Purchase Appraisals*, Dec. 2018, ("In addition, we explore a second GSE data set that provides appraisals and AVM estimates of originated loans along with performance outcomes (specifically, whether the loan became seriously delinquent). Supporting the view that reported appraisals frequently are biased upward, **we find that appraisals are somewhat less predictive of default than AVM estimates**." (emphasis added)); FHFA Staff Working Paper Series, *Appraisal Accuracy, Automated Valuation Models, and Credit Modeling in Rural Areas*, April 2018, ("After computing a set of AVM estimates using a hedonic model, we append them to a panel of Fannie Mae and Freddie Mac loan performance data. We initially use this combined dataset to explore the benefits of including an alternative measure of origination LTV, which may more accurately reflect initial borrower equity, when credit modeling. **We find that this alternative measure of LTV has a positive and statistically significant effect on the probability of future delinquency.** Further, this relationship is robust across a series of different specifications and functional forms." (emphasis added)); AVMetrics, *AVMs Keep Getting Better, Craig Gilbert Notices*, Jan. 2019 (At AVMetrics, we have been continuously testing AVMs for over 15 years, so we've seen how they've performed over time. As an example, the accompanying chart shows model performance accuracy as measured by mean absolute error, a statistical metric of valuation error. **We utilize many statistical measures of evaluating model accuracy and precision, and they all show significant improvement in AVMs over time. And, as these automated tools get better and the workforce of appraisers continues to shrink**, the FFIEC members' proposed change seems warranted, but that doesn't mean they don't have their critics." (emphasis added)).