MORTGAGE BANKERS ASSOCIATION

February 26, 2021

The Honorable Mark Calabria
Director
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20219

Re: Request for Information on Appraisal-Related Policies, Practices, and Processes

Dear Director Calabria:

The Mortgage Bankers Association (MBA)[1] appreciates the opportunity to comment on the Federal Housing Finance Agency's (FHFA) Request for Information (RFI) regarding appraisal-related policies, practices, and processes.[2] MBA supports the responsible integration of various approaches that improve the efficiency and accuracy of appraisal data collection and evaluation. FHFA's objective of promoting the modernization of the appraisal process is a welcome step toward determining the appropriate intersection of traditional evaluation methods and the incorporation of innovative digital tools.

As the mortgage finance industry continues to grapple with the effects of an aging appraiser population and longer turnaround times on appraisal findings, greater demand has been placed on identifying ways to automate aspects of the valuation process, while supporting the development of approaches that offer fair and unbiased results. Such an initiative requires close examination of the current appraisal process, the role of Automated Valuation Models (AVMs) and appraisal waivers in the housing market, opportunities to increase transparency and accessibility of property valuation

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 330,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets, to expand homeownership, and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 1,700 companies includes all elements of real estate finance: independent mortgage banks, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies, credit unions, and others in the mortgage lending field. For additional information, visit MBA's website: www.mba.org.

[2] FHFA, "Request for Information on Appraisal-Related Policies, Practices, and Processes," December 28, 2020. Available at: https://www.fhfa.gov/Media/PublicAffairs/PublicAffairsDocuments/RFI-Appraisal-Related-Policies.pdf.

data, and potential deficiencies within the appraisal infrastructure that may fail to detect, or perhaps even increase the risk of, racial bias.

<u>Appraisal Process Improvements</u>

Since the introduction of AVMs in the late 1990s, interest in developing methods to enhance appraisers' ability to access the data needed to offer an accurate opinion without physically entering a property has increased steadily. While MBA supports the ongoing development of such tools, MBA also acknowledges the need for appraisers and lenders to provide some level of oversight and due diligence to preserve the overall quality of the data referenced in future valuations. Any process improvements adopted by the industry must be comprehensive and employ a holistic view of appraisals that spans across origination, servicing, and loss mitigation activities.

It is within this context that FHFA must ensure that any advancements in technology proposed by Fannie Mae and Freddie Mac (the Enterprises) allow lenders, regardless of business model or size, to implement process improvements that do not inadvertently offer benefits to some while disadvantaging others. FHFA should not, for example, pursue sweeping policy changes that give preference to conventional products and thereby raise the costs associated with loans outside the Enterprises' footprints, such as portfolio loans or loans guaranteed or insured by the Federal Housing Administration, the Department of Veterans Affairs, or the Department of Agriculture. With respect to portfolio lending, it is also critical that the Federal Home Loan Banks be willing to provide advance funding on loans originated under alternative valuation approaches.

<u>The Role of AVMs in the Valuation Process</u>

In a response to a 2018 notice of proposed rulemaking by the federal banking regulators to revise the thresholds above which appraisals are required on residential real estate-related transactions, MBA submitted a white paper detailing the then-current state of AVMs.[3,4] By applying rules-based processes identified in the white paper, AVMs provide estimates of real estate values derived from statistical models using inputs from the property data collected. With developments in big data and machine learning, as well as improvements in the availability and integrity of data, AVM providers have advanced innovations in modeling and technologies. The

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[3] 83 FR 63110, "Real Estate Appraisals," December 7, 2018. Available at: https://www.federalregister.gov/documents/2018/12/07/2018-26507/real-estate-appraisals.

[4] MBA Valuation Analytics Workgroup, "The State of Automated Valuation Models in the Age of Big Data," January 2019. Available at: https://www.mba.org/Documents/Member%20White%20Papers/StateOfAutomatedValuationModels-final.pdf.

enhancements to real estate property data sources in terms of their geographic coverage, depth, and granularity — ranging from public records data to multiple listing services to tax, inspection, and mapping data — have enriched the inputs into the valuation models, leading to greater accuracy. The vast set of available data also allows modelers to analyze issues affecting properties from various angles; while recent sales transactions may be limited in some areas, AVMs can fill in data gaps by evaluating comparable properties over time and across various regions. As advances in data collection and digitization continue, the availability, accuracy, and performance of these models are expected to continue to improve.

AVMs play a critical role in the loan production process. AVMs are used to support evaluations, aid quality assurance review in originations, and assist as valuation assessments during post-origination processes. The real estate industry also has been moving towards greater use of digital mortgages, and therefore is becoming even more dependent on adapting newer technology and data, including AVMs. The shift towards digital mortgages enables faster processing times and cost savings to consumers and investors, allowing the industry to meet increasing consumer demands and expectations for a digital experience. Additionally, AVMs have helped to mitigate current constraints in the real estate industry related to the shortage of appraisal professionals available across the country. AVMs also ensure objectivity as the valuations, when paired with proper policies and guidelines, are produced systematically and without human interaction, reducing the potential for bias in the valuation process.

The real estate industry could benefit from expanding the responsible usage of AVMs, along with developing industry standards and guidelines. With the vast array of AVMs in the mortgage market, developing standards for their utilization would provide a framework for responsibly advancing the product. Understanding scenarios where and when AVM tools can be used most effectively will help in leveraging these tools. AVMs perform better, for example, where there are frequent sales transactions and with properties of typical size and quality. AVM validation must be conducted on a repeated and frequent basis to measure performance volatility. Validations also should be designed to gauge AVM performance across transaction types, property types, price tiers, and other criteria to understand the resiliency of the models. Effective AVM implementation also requires lenders' commitment to validation and vendor due diligence.

When used appropriately, AVMs can speed up the valuation and loan manufacturing timelines and significantly lower costs. Embracing process enhancements will benefit mortgage stakeholders and better allow consumers to achieve their homeownership goals.

The Impact of Appraisal Waivers

As the Enterprises continue to collect property data to support the effectiveness of AVMs and appraisal waivers, they should be cognizant that a sustained surge in mortgages originated without an in-person appraisal may dilute the quality of the data used in subsequent transactions. Should the market begin to rely too heavily on valuations not supported by traditional appraisals, lenders and the Enterprises may be exposed to greater risk because of a lack of evidence of the condition of a property.

Appraisal waivers, if not implemented properly, may create an unlevel playing field among lenders. The current appraisal waiver requirements differ between Fannie Mae and Freddie Mac — creating inconsistencies among institutions that rely on different Automated Underwriting Systems (AUS) for their findings. This disparity may result in one decision engine issuing more waivers than the other, providing an advantage to lenders who utilize the system that has more lenient requirements. It is for this reason that MBA recommends that FHFA ensure that the Enterprises use a transparent set of factors to determine when appraisal waivers are issued. This transparency will provide market participants with clarity regarding the criteria used by the Enterprises within the waiver process and help FHFA prevent a perceived advantage among AUS decision engines. Beyond the lender impact, investors are monitoring closely the prevalence of appraisal waivers, as well. To the extent that the use of these waivers is not consistent across the Enterprises, there could be an impact on the fungibility of Fannie Mae and Freddie Mac securities within the Uniform Mortgage-Backed Securities (UMBS) market.

Appraisal and property inspection waivers offer benefits to both lenders and borrowers by reducing costs and processing times. Despite these benefits, however, MBA strongly encourages FHFA to implement safeguards to protect the Enterprises, lenders, and borrowers from the unintended consequences of a market that overutilizes this option. FHFA can address these risks by requiring that the Enterprises use a transparent set of factors to determine when appraisal waivers are offered to lenders and borrowers, as well as establishing aligned supervisory limits on the frequency with which each Enterprise offers appraisal waivers. With respect to the factors that are considered, each Enterprise may weigh these factors differently in their internal algorithms, but the factors should be transparent to industry participants and borrowers.

Taken together, these supervisory measures would guard against excessive dilution of the appraisal databases, prohibit excessive use of waivers as a competitive tool, promote equal access to the secondary market for lenders, and better assure investors of aligned prepayment speeds in the UMBS market.

Uniform Appraisal Dataset Modernization

FHFA and the Enterprises currently are exploring significant changes to the Uniform Appraisal Dataset (UAD) and the corresponding forms. MBA supports updates to the UAD that result in more efficient processes, lower costs, and greater accuracy in property valuations. Because the recommended changes to the UAD require a financial investment by the impacted parties, MBA believes that the costs of any such changes should be balanced against the anticipated benefits. At this time, the Enterprises have not provided enough information for the lending community to evaluate whether each of the proposed changes will provide a benefit to the parties involved.

Through engagement in the Enterprise Appraisal Advisory Group and the Mortgage Industry Standards Maintenance Organization (MISMO), MBA is aware that the Enterprises are proposing substantial changes to the UAD. Such an expansion of the UAD is likely to result in high initial implementation costs for the lending community, which could result in higher appraisal costs for borrowers.

Revisions to the Uniform Residential Appraisal Report (URAR) and the data that is collected will affect many internal lender processes, including underwriting and quality control. Many lenders also have operational processes that input, process, and assess the property-level information obtained through the appraisal. Changes to the appraisal process will require changes to the internal operations of these organizations. Importantly, many of the proposed changes are not backwardly compatible with the data that has been collected for the past decade. This will require substantial modifications to systems in use today — both in the format of the information and the rules and logic employed. In addition, the lack of backwards compatibility will severely impact analytics and research performed on historical datasets. While the impact and cost to different lenders and market participants may vary widely, it is critical that these effects be considered as the initiative is developed and executed.

Ongoing concerns center on the fact that the value of the proposed changes either has not been assessed fully or has not been shared with the lending community and its vendors. At this stage, lenders and vendors do not have a clear understanding of the benefits that will accrue or the consequences that may arise from the Enterprises' initiative.

As such, MBA encourages the Enterprises to provide the mortgage finance community with more details regarding the expected benefits of these changes. The Enterprises should establish more formal communications with a broader set of industry participants to determine how these benefits compare to the estimated costs to implement and support these changes. For proposed changes where the potential benefits cannot yet be determined, MBA recommends that the Enterprises develop small-scale, cost-effective pilot projects involving a representative mix of primary market lenders and vendors. These pilot projects would assess the value of these changes and narrow the end-state data expansion to those fields that have demonstrated value in improving appraisal accuracy and reliability.

MBA further recommends that the Enterprises and FHFA consider limited implementation or additional pilot-testing of the revised UAD before it takes effect — a step that would allow for appropriate refinements prior to full execution.

Public Accessibility of Enterprise Collateral Data

In the decade since the launch of the Uniform Mortgage Data Program, the Enterprises have invested tremendous resources in the collection and analysis of loan-level data covering several dimensions of the market, and lenders have invested similarly to comply with these new demands from the Enterprises. The creation of the Uniform Collateral Data Portal and the UAD, as well as the significant improvements made to the accuracy, integrity, and quality control processes with respect to collateral data represent important achievements by FHFA and the Enterprises.

As with many other data enhancements instituted by the Enterprises, much of the improved collateral data has not been made publicly available and remains accessible only to FHFA and the Enterprises themselves. The limits on access to this collateral data are especially noteworthy, as many industry participants have contributed to the collection and development of this higher-quality data. These contributions have come from market participants' individual efforts as well as through collective efforts under the auspices of standards-setting bodies such as MISMO.

Access to the Enterprises' collateral data would provide market participants with far more detailed information on property-level valuations than they can collect or obtain today. As such, broader availability of this data holds the potential to improve risk management approaches, enhance forecasting tools, and better determine how valuations differ across geographies and various borrower demographic factors. These expanded capabilities should not be the exclusive property of the Enterprises, or even the exclusive domain of industry participants. The Enterprises' collateral data instead should be available broadly to any interested stakeholders, including public- and private-sector researchers.

Increased access to this data would be consistent with the Enterprises' charters as well as FHFA's statutory responsibility to provide public access to Enterprise mortgage data. A more transparent approach to this data also would improve risk analysis and modeling by Enterprise counterparties, thereby strengthening the

Enterprises from a safety-and-soundness perspective. Together, these considerations point to the need for FHFA to develop a process by which the Enterprises' collateral data can be shared with public stakeholders on an ongoing basis. Such a process, if implemented in a manner that makes this data accessible without unnecessary restrictions or barriers, is likely to provide important benefits throughout the housing finance system.

Protecting Against Racial Bias in the Appraisal Process

The residual effects of systemic racism and redlining embedded in historical property values are apparent, and research on the breadth of their impacts on communities of color continues to develop. This research includes the frequency with which property values are suppressed in areas with larger populations of potential minority borrowers. Suppressed valuations, even with respect to renovated properties, may exacerbate "appraisal gaps" that result in fewer homeownership opportunities. In the interim, MBA is working to identify opportunities to mitigate the potential for current appraisal practices to disadvantage minority borrowers.

Within the appraisal waiver process, MBA recommends that FHFA instruct the Enterprises to implement waiver requirements in a manner that minimizes the potential for any adverse impact on minority borrowers. Generational wealth, for example, is less frequently a resource for home purchases in communities of color. The potential over-emphasis of factors such as exceptionally low loan-to-value (LTV) ratios, if they eclipse other borrower criteria that may be less stratified by race, may benefit applicants with access to greater resources for a large down payment. Similarly, the wage and income gaps among minority and white borrowers may impact average sales prices and loan amounts — with black and brown borrowers obtaining smaller-balance mortgages, on average, than their white counterparts. Again, if the Enterprises place too great an emphasis on mortgage amounts when determining eligibility for appraisal waivers, minority borrowers are likely to face increased costs.

MBA further recommends that FHFA consider supporting the Enterprises' incorporation of virtual evaluation tools, when feasible, to reduce the potential for bias during the collection and analysis of property data. Cutting-edge three-dimensional and artificial intelligence software are being developed that collect pertinent data such as property type, square footage, condition, and notable interior enhancements while excluding any personally identifying information that would suggest the race or ethnicity of the borrower. These tools hold great potential to help avert intentional or unintentional consideration of borrower race or ethnicity (and potentially other inappropriate factors) when valuing a property.

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MBA firmly believes that a comprehensive appraisal modernization implementation strategy that considers the above observations and recommendations will greatly improve the overall efficiency of the appraisal process. MBA also acknowledges FHFA's objective of supporting safe and sound lending practices that promote integrity and fairness. In order to do so, FHFA should encourage the Enterprises to adopt a modernized appraisal process that delivers reliable property valuations, which in turn will contribute to the success and overall health of the housing finance system.

Thank you in advance for your consideration of these comments. Should you have questions or wish to discuss further, please contact Julienne Joseph, Associate Director of Government Housing Programs and Member Engagement, at (202) 557-2782 and jjoseph@mba.org.

Sincerely,

Robert D. Broeksmit, CMB
President and Chief Executive Officer
Mortgage Bankers Association