



August 21, 2023

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

ATTN: Comments/RIN 2590-AA62, Quality Control Standards for Automated Valuation Models

Dear Director Thompson,

U.S. Mortgage Insurers (USMI) and our member companies¹ appreciate the opportunity to provide feedback on the Notice of Proposed Rulemaking (NPR) on “Quality Control Standards for Automated Valuation Models”² that was jointly issued by the Office of the Comptroller of the Currency (OCC), U.S. Department of the Treasury, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation (FDIC), National Credit Union Administration (NCUA), Consumer Financial Protection Bureau (CFPB), and Federal Housing Finance Agency (FHFA) (collectively “the Agencies”). USMI represents the nation’s leading private mortgage insurance (MI) companies, and our members are committed to a strong housing finance system backed by private capital that enables access to affordable and sustainable mortgage finance for all home-ready borrowers.

As sophisticated long-term managers of single family mortgage credit risk, private MIs support a workable regulatory framework for mortgage market participants’ use of automated valuation models (AVMs) and policies that appropriately balance improvements and efficiencies in the collateral valuation process with the accurate assessment and pricing of risk. The private MI industry recognizes that there are opportunities to modernize residential property valuation with the use of AVMs, but it is critical that appropriate transparency, monitoring, and governance are in place. Innovation in collateral valuation, including the growing use of AVMs in the primary and secondary mortgage markets, must include proper guardrails, transparent standards, and appropriate protections from undue credit risk in the housing finance system.

The NPR fulfills the *Dodd-Frank Wall Street Reform and Consumer Protection Act*’s requirement³ that the Agencies, in consultation with the Appraisal Subcommittee and Appraisal Foundation, promulgate a rule to ensure the integrity of AVMs in single family mortgage lending and securitization. It specifically would require covered entities to adopt and maintain quality control standards “for the use of automated valuation models in determining the value of collateral in connection with making a credit decision or covered securitization determination regarding a mortgage or mortgage-backed security.”⁴ AVMs are used by a wide variety of

¹ USMI membership comprises the following private mortgage insurers: Enact Mortgage Insurance Corporation; Essent Guaranty, Inc.; Mortgage Guaranty Insurance Corporation; National Mortgage Insurance Corporation; and Radian Guaranty, Inc.

² 88 Federal Register 40638 (June 21, 2023).

³ 12 USC 3354

⁴ Proposed FHFA regulation at 88 Federal Register 40674 (June 21, 2023).



mortgage market participants, including Fannie Mae and Freddie Mac (the GSEs), lenders, investors, and issuers, and USMI fully supports policies that promote accuracy in algorithmic valuations, compliance with nondiscrimination laws and regulations, and the safety and soundness of the U.S. housing finance system. Further, the Agencies’ regulatory frameworks should apply transparent and consistent requirements for their regulated entities’ use of AVMs to prevent any inappropriate or unintended competitive advantage.

Principles-Based Approach to Quality Control Frameworks

The NPR would require covered entities to “adopt and maintain policies, practices, procedures, and control system to ensure that automated valuation models used in [] transactions adhere to quality control standards” that promote accuracy and facilitate compliance with applicable nondiscrimination laws and regulations.⁵ It outlines a principles-based framework that does not prescribe detailed or rigid requirements but rather grants covered entities the flexibility to establish and maintain their own quality control standards and frameworks. The Agencies specifically state that the NPR “provides institutions the flexibility to tailor their quality control standards for AVMs as appropriate based on the size of the institutions and the risk and complexity of transactions for which they will use covered AVMs.”⁶ While a principles-based framework can promote innovation and competition in the housing finance system, it is paramount that it be balanced with guardrails that ensure robust quality control standards and prevent a competitive race to the bottom. USMI encourages the Agencies to include in the final rule additional guidance for covered entities’ compliance with the regulation, including a set of best practices, issues observed with the use of AVMs, compliance expectations, and potential enforcement actions.

Application to the GSEs

The NPR stipulates that a covered securitization determination includes “whether to waive an appraisal requirement for a mortgage origination in connection with its potential sale or transfer to a secondary market issuer.”⁷ USMI supports the inclusion of the GSEs for the application of the proposed rule as they are two of the largest users and managers of AVMs.⁸ The GSEs use AVMs and other valuation technologies to determine property valuation at origination, as well as throughout the mortgage lifecycle to support portfolio management, conduct quality control processes, and evaluate credit enhancement needs. Considering the GSEs maintain separate proprietary AVMs, the lack of alignment in their coverage, variances associated with confidence levels, lack of transparency to market participants, and inconsistencies in competing models could, absent appropriate safeguards, lead to borrowers being treated disparately based on which GSE acquires a given loan and make it more difficult to prudently manage credit risk. FHFA’s oversight of the GSEs’ AVM quality control standards must prevent disparate treatment of borrowers between the two GSEs and a race to the bottom by addressing the potential for “gaming” which can incorrectly value collateral and negatively impact credit risk pricing and management.

⁵ Proposed FHFA regulation at 88 Federal Register 40674-5 (June 21, 2023).

⁶ 88 Federal Register 40659 (June 21, 2023).

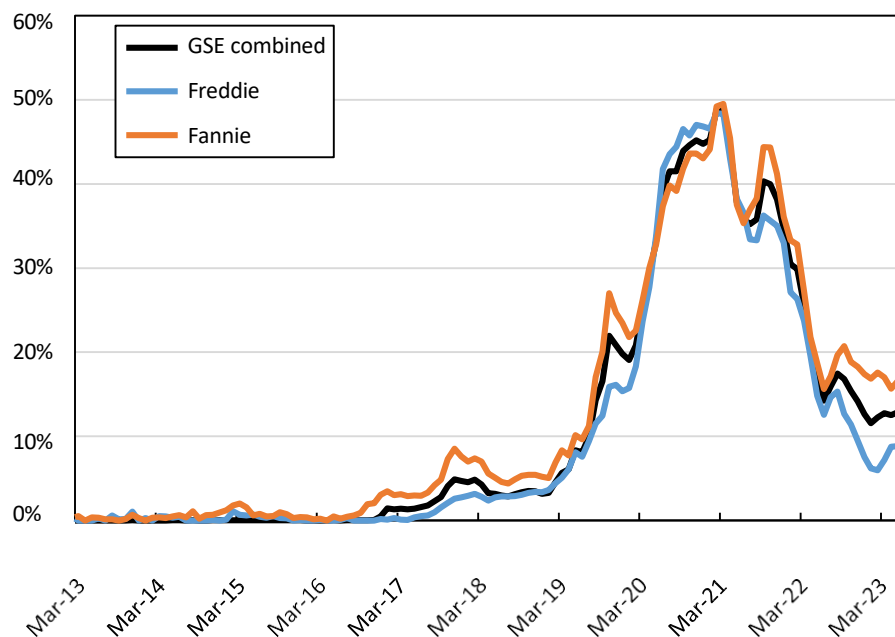
⁷ Proposed FHFA regulation at 88 Federal Register 40674 (June 21, 2023).

⁸ 88 Federal Register 40643 (June 21, 2023).

There is significant value for the safety and soundness of the housing finance system for FHFA to ensure the GSEs have appropriate quality control frameworks in place should they consider expanded applications of AVMs, including in the areas of offering loss mitigation options and any changes to credit enhancement policies. For example, as AVMs are designed to be predictive in aggregate at specified confidence intervals, solely relying on AVMs absent robust guardrails for the purposes of determining collateral valuation may lead to the GSEs inappropriately acquiring loans without required credit enhancement, in contravention of their congressional charters. Likewise, USMI believes that the current GSE policies⁹ requiring an appraisal or broker price opinion (BPO) for borrower-initiated cancellation of private MI based on current property value is an important safeguard against adverse selection and undue credit risk in the housing finance system.

A specific current example of the GSEs’ use of AVMs and other valuation technologies is the application of appraisal waivers for certain mortgage transactions.¹⁰ The use of appraisal waivers fluctuates throughout the market cycle and has been used by the GSEs to respond to rapid runups in borrower demand and/or events such as the COVID-19 pandemic that presented issues for in-person full appraisals. Currently, only about 12% of loans acquired by the GSEs receive an appraisal waiver (with a significant difference between Fannie Mae and Freddie Mac) but their usage spiked to almost 50% in March 2021, with the non cash-out refinance segment of the market peaking at nearly 70%.¹¹

Share of GSE loans with appraisal waiver, by guarantor

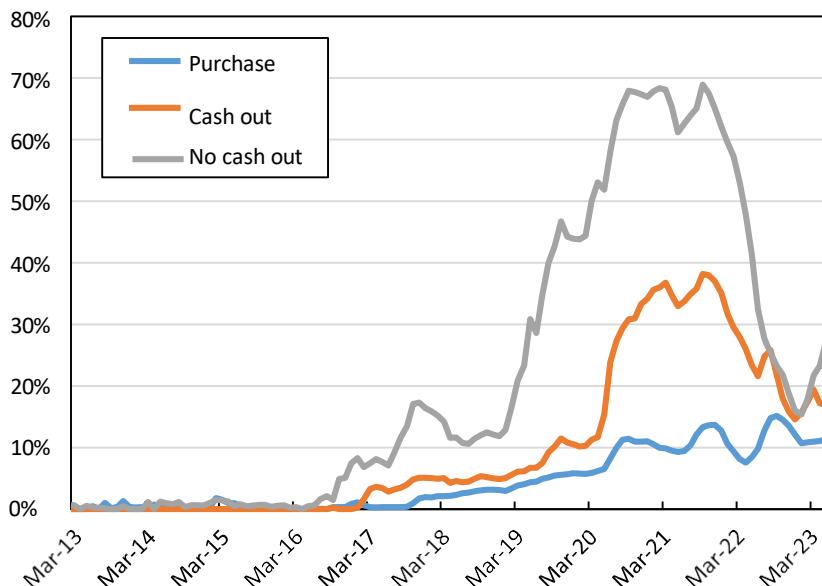


⁹ Fannie Mae Servicing Guide 8203.2 and Freddie Mac Servicing Guide B-8.1-04.

¹⁰ 88 Federal Register 40643 (June 21, 2023).

¹¹ American Enterprise Institute (AEI) Housing Center, “[Prevalence of Appraisal Waivers \(June 2023\)](#)” (August 21, 2023).

Share of GSE loans with appraisal waiver, by loan purpose



USMI has routinely noted that the GSEs’ use of AVMs for appraisal waivers warrants particular attention and oversight, especially for high loan-to-value (LTV) mortgage transactions. Appraisal waivers and the use of AVMs can materially impact LTV, eligibility, pricing, capital requirements, and risk assessments associated with GSE and private MI operations. AVM accuracy is particularly important for higher LTV mortgages since the margin for error is less due to smaller equity cushions and an incorrect valuation could expose the GSEs, taxpayers, and housing finance system to greater credit risk.¹² Further potential for increased taxpayer risk exists if an AVM produces a property valuation that misprices or eliminates loan-level private MI credit protection.

Transparency in AVM Data

Despite the GSEs’ extensive use of proprietary AVMs and their centrality in the \$6.6 trillion single family conventional market,¹³ housing finance stakeholders currently have no insight into their underlying methodologies and historical data. USMI has consistently advocated¹⁴ for data democratization in the conventional mortgage market, particularly around a better understanding of how the GSEs leverage data in their valuation decision processes. Making data available to market participants who contribute to the valuation analysis and are part of the underwriting process, including appraisers and appraisal management companies, lenders, private MIs, title insurance companies, investors, and data analytics providers, will assist these participants in their analyses of individual mortgage transactions. FHFA should increase transparency for market participants by requiring the GSE to further democratize valuation data with access similar to Fannie Mae’s Data Dynamics® and Freddie Mac’s Clarity Data Intelligence® that serve as

¹² There is a material difference in an AVM producing a slightly incorrect valuation on a 60% LTV loan with an equity cushion of 40% than an incorrect valuation on a 90% or 95% LTV mortgage.

¹³ As of June 30, 2023 according to 2Q2023 GSE filings.

¹⁴ USMI, “[Guardrails for Appraisal Modernization](#)” (June 2022).



centralized hubs for vast amounts of credit risk transfer (CRT), mortgage-backed security (MBS), and historical loan performance data.¹⁵

Requested information would include the tolerances that are coded into the GSEs' AVMs, statistical thresholds for the underlying methodologies, established limits on and basis for standard deviation, and clear protocols for the treatment of loans that fall outside of established parameters. Data democratization would greatly enhance transparency within the housing finance system and improve risk management practices and strategies across the market. Further, USMI urges FHFA to require the GSEs to issue periodic reports on their use of AVMs and trends related to undervaluation and overvaluation.

Nondiscrimination and Fair Lending

The private MI industry fully supports robust compliance with and the Agencies' enforcement of applicable nondiscrimination and fair lending statutes and regulations to ensure that all home-ready borrowers, regardless of race, ethnicity, gender, age, or other protected class, have access to affordable and sustainable mortgage financing. Sustainable homeownership remains the primary vehicle for families to achieve financial stability and build long-term, intergenerational wealth and USMI supports policies that ensure property valuations, including those concerning AVMs, responsibly promote homeownership opportunities, especially for homebuyers who lack access to large down payments.

USMI appreciates the opportunity to share its views on this NPR and we welcome any questions you may have concerning our observations and recommendations. Please do not hesitate to contact me at sappleton@usmi.org or 202-280-1820 for additional information related to this submission.

Very truly yours,

A handwritten signature in blue ink, appearing to read "Seth D. Appleton", with a long horizontal flourish extending to the right.

Seth D. Appleton
President
U.S. Mortgage Insurers

¹⁵ <https://capitalmarkets.fanniemae.com/tools-applications/data-dynamics> and <https://capitalmarkets.freddiemac.com/crt/clarity>.