

Federal Reserve Board – Docket No. OP-1338
20th Street and Constitution Avenue, NW
Washington, DC 20551

Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

VIA EMAIL

January 16, 2009

Comments Re: Proposed Interagency Appraisal and Evaluation Guidelines

To All Concerned:

I submit the following comments as feedback to the proposed “guidelines”. My experience includes 29 years in the appraisal industry as a residential and commercial fee appraiser, lender (thrift, federal and state bank) production and review appraiser, and currently as state chartered bank chief appraiser. My reputation is positive, I have never been rated unsatisfactory in an audit, I have never been sued, and my professional opinion has repeatedly been sought individually and/or publicly as a guest speaker.

These are my personal comments and do not necessarily reflect those of my employer. I will attempt to put forth my comments and feedback suggestions in the order in which the topic is discussed in the proposed guidelines.

Vagueness

I realize the new guidelines, like the old ones, were left purposely vague as regulators often indicate disinterest in dictating, formulating and/or managing business practices. However, after recent events in the financial markets related to under-regulated or under-enforced collateral-based lending compliance procedures, I was hoping for more “teeth” in these new and expanded guidelines. This is especially relevant in sections that were not just a compilation of prior policies and guidelines but actually added or expanded sections.

In my interactions with loan production officers and managers, regulatory “wobble words” with potential alternate interpretations - such as using “should” instead of “must” - are open doors to permit softening of the regulatory intent and a slippery slope toward gray area process interpretations that can lead to taxpayer losses. When financial markets are positive and creative lenders look for new business prospects and expanding customer base or market share, these “wobble words” allow loose interpretation with the opportunity to open that door – as observed recently in cases of alternative mortgage products with insufficient underwriting and valuation, short-cut appraisals and opinions (BPOs, AVMs, and other valuation opinions that were less than full appraisals) in complex or higher risk situations, lender avoidance of impropriety with appraiser independence by deferring to under-regulated mortgage brokers or AMCs to be the “heavy”, interpretation of lower versus higher risk, interpretation of who may (and who may not) engage appraisers, etc. There are lenders who may wait to be caught as the punishment is often less severe than the profit to be taken (recall the Ford “Pinto” case as a prior example of corporate cost-benefit analysis gone wrong, or note the current economic crisis), especially if portfolios are sold to investors and the originating lending officers are insulated or long gone. All “wobble words” MUST be removed – either the guidelines will be enforceable with the compliance intent of the regulators (“must”, “required” or “expectation”) or they will not (“shall”,

“should”, “may” or “remind”). If the intent is not to enforce compliance but rather to make suggestions on best practices, maybe this is the wrong document for such advisory opinions.

Appraisal Development and Appraisal Reports

Proposed guidelines are softly (“should”) requiring institutions to “discuss its needs and expectations for the appraisal with the appraiser” while no longer accepting defined USPAP reporting formats (Standard 2-2) as Scope of Work parameters. This puts a great deal of burden on smaller lenders that do not have adequate internal appraisal experts to be on equal footing with their fee appraisers in understanding USPAP and what should or should not be presented in an appraisal, and it appears to confuse appraisal development process (Standard 1) with appraisal reporting (Standard 2). This section might better serve as a more detailed guideline to lenders on a) requiring dialogue with the appraiser on what information and analyses would best assist the lender to support their loan or credit decision, and b) suggesting dialogue with the appraiser regarding what reporting format might best present the desired information and analyses based on the complexity of the assignment. To do so requires expanded regulatory guide notes, aimed at smaller lenders without internal appraisal expertise, that examine different situations as examples or outlines of how such dialogue might go and what are the relevant questions to ask of the appraiser.

Reviewing Appraisals and Evaluations

On page 14 (and similar wording on page 38) the proposed guidelines state “that an institution *with prior approval from its primary regulator* [italics added] may employ various techniques, such as automated tools or sampling methods, for performing pre-funding reviews of appraisals or valuations supporting lower risk single-family residential mortgages.” That sentence is full of potentially huge issues that need better clarity.

First, “prior approval” is prohibitive and contrary to best practices in many instances. A lender cannot be expected to stop or slow a customer’s loan process down to wait for authorization from a regulator which probably – based on my experience – will likely be too vague (see first section) to have been worth the wait. As an example, it would be non-competitive for one lender to have to wait for “prior approval” from their regulator to determine if an AVM might be acceptable in reviewing an appraisal for a HELOC (quick turnaround loan), especially if this review tool was already approved for other lenders. Prior approval must be provided within this guideline document, or disallowed. If it is permitted for one lender it should be good for all so as to avoid the appearance of discriminatory or disparate practice (with or without intent), or preferential treatment.

Second, “automated tools or sampling methods” should be defined. What specifically is and is not permitted?

Third, “pre-funding reviews of appraisals or evaluations supporting lower risk single-family residential mortgages” should probably be performed differently and not lumped together in combined instructions. If something less than an appraisal is permitted, then the risk level is inherently low – or the regulatory deminimus must be revised back down to the point of “low risk”. Review guidelines for appraisals should not coincide with those for evaluations.

Appraisal and Evaluation Program

Page 19 lists what should be included in this program of policies and procedures. One of the listed items merits further detail – “Establish selection criteria and procedures to evaluate and monitor the ongoing performance of persons who perform appraisals or evaluations”.

How can this be enforced upon third party AMCs (appraisal management companies that control the engagement process and are not currently regulated), or with one-off shopped loans (agent shops loan package that includes a completed agent-engaged appraisal with intended use for FIRREA compliance, yet from an appraiser not already on a lender's approved fee panel), or with transferred loans (first lender did not make the loan but ordered the appraisal, and it is submitted to second lender who does not have a relationship with the appraiser), or with participation loans (non-lead participant has no relationship with the appraiser)? All of these situations may entail the lender having to make a decision on an appraisal wherein they or their agent may not have directly engaged the appraiser for the institution so there is no "ongoing performance" to evaluate and monitor.

Further, the "selection criteria and procedures" of one lender or agent who engages the appraiser may be considered wholly insufficient to the eventual lender considering the loan package that includes the appraisal. Perhaps minimum due diligence guidelines should be proffered by the regulators as a minimum standard for prequalifying acceptable appraisers, other than by virtue of being adequately licensed (e.g., in-file review of redacted work samples, resume, minimum work experience years, minimum education level and/or supervised on-the-job training, documented positive references, required file review notes of internal due diligence findings, etc.).

Independence...

On page 20 the new guidelines remind that persons who perform appraisals, or evaluations, must be independent of loan production and collection processes or have any interest in the property or transaction. It continues to note what an institution may or may not communicate to the appraiser. However, it does not go far enough. Since mortgage brokers are often the source of loan packages, often including appraisals engaged by the mortgage broker – supposedly acting as agent for the lender – they, too, should be regulated with respect to appraiser independence. Agents (mortgage brokers) must also be indicated within the guidelines as representatives of the lender who are not permitted (strong language) to violate appraiser independence in any manner. HVCC goes so far as to not let a lender doing work for the GSEs to accept an appraisal where a mortgage broker was involved in the engagement, process or delivery in any way other than perhaps as a source of property or transactional information that may not otherwise be obtainable. While mortgage brokers may not yet be regulated by federal regulatory agencies, lenders who do business with these "agents" do fall under jurisdiction and must be instructed on what is and is not acceptable when it comes to letting "agents" act on their behalf. This is most notable when the "agency" relationship does not begin until after an appraisal has already been engaged and produced, wherein the agent is in actuality acting on behalf of the borrower and then later assumes lender agency status once submitting a loan package to a lender. Independence of the Appraisal and Evaluation functions must be held sacrosanct and inviolable by lenders and their agents.

Selection of Persons Who May Perform Appraisals and Evaluations

Once again, the agency loophole is evident in this section. "An institution or its agent must directly select and engage appraisers." This conflicts with HVCC as these guidelines offer a less stringent rule wherein it is acceptable for an agent, presumably a mortgage broker, to engage the appraiser and deliver the appraisal to the prospective lender.

"The person who selects or oversees the selection of appraisers or persons providing evaluation services should be independent from the loan production area. Independence is compromised when a borrower or loan production personnel recommends or selects a person to perform an appraisal or evaluation."

While an institution is directed not to use borrower-ordered appraisals, mortgage brokers – initially acting as borrower agents – are permitted to select the appraiser, and lenders are currently allowed to accept these appraisals if they appear to conform to regulatory compliance, provide credible results, and otherwise meet said lender’s standards even if the appraiser or engagement particulars are not known to the lender. This conflicts with these guidelines’ intent of appraiser independence from loan production personnel. Mortgage brokers ARE essentially the first line of loan production whose income is tied directly to the appraisal results and loan decision, and must be excluded by these guidelines from any and all parts of the appraisal engagement and development processes for all property types and prospective loan decisions.

Minimum Appraisal Standards

On page 24 it says the appraisal must “be written and contain sufficient information and analysis to support the institution’s decision to engage in the transaction.” It would be useful if the guidelines indicate to whom this is directed – in the opinion of the appraiser or the lender? An appraiser may complete the assignment and offer what that appraiser believes is “sufficient information and analysis” for a typical lender, yet the specific lender may need more information for various reasons (i.e., weak credit needs stronger collateral value confidence or appraiser’s inherent but unspoken or unwritten professional knowledge may exceed the comprehension of the lender utilizing the appraisal report). This section could be enhanced to indicate who has the final say on what is sufficient, especially considering that the appraiser already has the final say on the scope of work and that non-loan production staff may not be as well versed as to know what to discuss with the appraiser upfront to ensure an appropriate scope of work for the assignment.

Page 25 “Proposed Construction or Renovation” paragraph states that “an institution may request a prospective market value as completed and as stabilized”. These guidelines should clearly indicate when to obtain a prospective (future) market value or a hypothetical (current, or anytime based on hypothetical conditions) value in a proposed construction appraisal. In practice, all proposed construction assignments typically request “as is” and prospective values; however, the exception is that residential subdivisions typically request “as is” and hypothetical (current) values. This discrepancy should be discussed and the inherent inconsistency and confusion laid to rest by virtue of a definitive regulatory guideline or policy as to which value is correct for compliance or at least preferred.

The “12 month” rule remains unclear. The last sentence under “Attached or Detached Single-family Homes” on page 27 is confusing – does it mean that those units that could be sold in less than 12 months may be supported by the appraisal of the individual units without discounting, yet those expected to take more than 12 months must include deductions and discounts, or do all remaining units need to reflect discounting and deductions? How does the rule apply to OREO subdivisions where the loan has been removed and all that remains is completion, if necessary, and sellout of remaining units?

On page 28 the guidelines note that “market value should not include a going concern value or a special value to a specific property user. An appraisal may contain separate opinions of value for such items so long as they are clearly identified and disclosed.” To what extent should these values be supported or derived in the appraisal to adequately delineate from tangible market values? For example, appraisal of nursing homes includes an entity’s value comprised typically of tangible real estate value, tangible value of furnishings and equipment, and intangible business or going concern value to a specific property user; these values, when segregated, are usually arbitrarily derived by comparing the income approach value to the cost approach component values of real estate, FF&E, and remaining overage value (BEV) yet these component values may vary significantly at older facilities (excessive depreciation weakens

reliability) or in mature communities (lack of accurate land value). Perhaps some expanded guidance is merited here.

There exists little to no guidance with respect to work-out (loan modification through NOD) or foreclosure appraisal or evaluation assignments, or to lenders with respect to related scope of work issues. Other than defined terms for market values and liquidation values, there are no sufficient definitions for a) foreclosure market value where the majority of the market participants are not willing sellers as most are under duress to accept a quicker than typical purchase offer, short-sale, or other price that is not reflective of true market value between willing buyer and seller; b) soft market value where there are few to no qualified buyers or financing is unavailable so there are very few consummated transactions within a reasonable time frame from which to adequately estimate value for the subject; c) bankruptcy value where the current seller is under duress yet the market is not; d) pre-foreclosure value where the property is about to go into foreclosure yet the lender needs an updated value for filing the NOD (Notice of Default) which may include provisions for repairs and sales costs; and e) OREO value where the institution owns the property and must consider value for monitoring, reporting, and/or marketing purposes (these may be different value considerations than pre-foreclosure). OREO value should reflect the fact that there is no longer a loan in place, so a 12-month sellout consideration (page 27) on an incomplete subdivision project should not be back-dated to the original date of funding but rather the time frame should reflect the current date of value through the anticipated sellout of the project when considering discounts applicable to the valuation. There may be other values to consider defining.

Reviewing Appraisals and Evaluations

At the top of page 37 the new guidelines state, “This review should be performed prior to the final credit decision and ensure that the appraisal or evaluation adequately supports approval of the credit.” In that a few institutions saw fit to obtain an appraisal and/or review for compliance sake but did not care if it was completed after funding the credit, this sentence should probably be slightly revised – for semantics – to say “should be *completed* prior to the final credit decision *and/or funding*...”.

Program Compliance

The term “controls” should be defined or described for clarity of intent.

The second paragraph is confusing due to the indiscriminate use of the term “evaluation”. For clarity, “collateral” evaluation should be distinguished from “periodic” evaluation of appraisers, and from “service provider” evaluation with respect to retention of the appraiser or person performing a collateral evaluation.

Portfolio Monitoring and Updating Collateral Valuations

This section recommends that each institution install a prudent portfolio monitoring program, however it does not clearly define what is considered “prudent”. For example, markets may weaken but if the credit continues to perform as agreed then why would a lender find it prudent to spend lender (stakeholder) funds updating the collateral valuation? This is especially relevant when the market temporarily weakens in a downward economic cycle yet it is anticipated that an upward cycle will soon improve the equity position of a property and borrower that are performing as agreed.

Appendix A – Appraisal Exemption #1: Appraisal Threshold

In light of the recent financial crises in large part perpetuated by insufficient collateral valuation support for sub-deminimus transactions, it seems prudent (as regulators expect of their member institutions) at

this time for each regulatory agency lower their appraisal threshold exemption to return to a point of well-managed risk.

Appendix A – Appraisal Exemptions #9 and #10: Transactions Insured or Guaranteed by a U.S. Government Agency or U.S. Government-sponsored Agency, and Transactions that Qualify for Sale to, or Meet the Appraisal Standards of, a U.S. Government Agency or U.S. Government-sponsored Agency

Now that the GSEs must report to the taxpayers through government ownership, they must fall subject to FIRREA, USPAP, and these and other regulatory compliance guidelines. Similarly, the exemptions (#9 and #10 of thirteen exemptions) for transactions insured or guaranteed by or for sale to U.S. government agencies and/or GSEs is a loophole that must be closed. Taxpayers must be protected to the fullest extent without carve-outs. Problems arising from these exemptions take in the financial difficulties of the GSEs, the need for development of a Home Valuation Code of Conduct to stem a lawsuit with the state of New York, the need for multiple appraisal forms to suit each government agency or GSE or regulated lender, and difficulty in interpreting and enforcing appraisal rules that are good for one but not all agencies.

Appendix A – Appraisal Exemption #13: Transactions Involving Underwriting or Dealing in Mortgage-backed Securities

Clearly this exemption needs to be reconsidered, and probably rescinded or significantly modified, in light of the recent collapse of the MBS industry.

Appendix C – Glossary: Insufficiently Defined Terms

- Agent
 - The glossary should define if an agent may act on behalf of both borrower and lender (potential conflict of interest), and if so should this agent (usually mortgage broker) be permitted to engage appraisers?
 - May an agent be defined as someone who brings business to the lender (acting on their own, a borrower's, or another lender's behalf), or should it be limited to reflect someone explicitly acting on behalf of the lender to solicit business – focus being on who is represented as the primary client? This needs clarity.
 - Can or should a mortgage broker who brings a one-off transaction to a lender – possibly after shopping it around – be considered an agent for that lender?
 - Guidelines say “an institution's policies and controls should ensure that the institution does not communicate a predetermined, expected, qualifying, or owner's estimate of value, or a loan amount or target LTV to a person performing an appraisal or evaluation.” However, what is to prevent the under-regulated agent from pressuring the appraiser, or just providing leading information?
 - If a lender's agent “must directly select and engage appraisers” and the agent is a mortgage broker shopping a loan package, then how can the eventual lender be assured the “person who selects and oversees the selection of appraisers” is “independent from the loan production area”? This conflicts directly with (and is weaker than) the proposed HVCC in which it completely disallows a mortgage broker from engaging or selecting an appraiser.
- Approved Appraiser List
 - With respect to AMCs, this definition should be made broader to take in lists maintained and/or compiled by third party vendors that are utilized by lenders.
 - Without any minimum due diligence standards or guidelines in place, what is considered “approved” by one institution may be considered negligent due diligence by another. Perhaps a minimum prequalification standard for “approval” (and similarly “do not use”)

lists of appraisal vendors should be established beyond the simple licensing requirements of FIRREA and AQB.

- Exposure Time + Marketing Time
 - These terms should be eliminated as obsolete. Their intent is good, yet USPAP does not mandate either be put into an oral or written appraisal report (Exposure Time is to be considered in the appraisal process, but not in the reporting; Marketing Time is not referenced in USPAP anymore, though it is still referenced in an Advisory Opinion). In a rapidly changing market environment, these terms have no merit. For example, a property appraised in mid to late 2007 with a reasonable-at-the-time 6-12 month Marketing Time estimate proved to be erroneous by early 2008 when valuation with a similar 6-12 month Exposure Time (periods overlapping) would be completely contradictory due to the unexpectedly rapid market value deterioration during that period of time. These terms do not provide sufficient value-add to the appraisal or loan decision process and at times may be misleading as noted in the example above.
- Federally Related Transaction + Real Estate-Related Financial Transaction
 - These terms are essentially redundant. It is unnecessary to have two terms that mean the same thing. These should be merged into a single term, with term modification applicable only when referencing non-real estate related credit-only federally related transactions (perhaps coined as Credit-only FRTs).
- Loan Production Staff
 - Definition is unclear as it refers to “any employee whose compensation is based on loan volume”, yet anyone working at a financial services institution has compensation based on loan volume directly or indirectly. If only referring to direct compensation based on loan volume, it should be noted that subordinates to loan volume-generating staff (e.g., processors, funders, loan assistants, etc.) rarely are compensated based on volume but rather on fixed wage. This definition also seems to inexplicably exclude “agents” whose compensation is directly dependent on loan volume. This definition must be made clearer.
- Prospective Market Value
 - This definition should be slightly more precise as to whether “current expectations and perceptions of market participants, based on available data” shall reflect current estimates of future value based on current economics, or on forecasted economics foreseeable from available data to the anticipated future date of completion (or stabilization). The former would reflect a hypothetical situation assuming future economics are the same as the current date of value without considerations for inflation/deflation or changing costs/prices/expenses to the prospective date of value, or other possible cyclical economic considerations. The latter suggests the value would be adjusted up or down to reflect anticipated economic considerations up to the point of completion (or stabilization), possibly also considering time value of money. This added regulatory clarity would enhance the appraisal function by unifying methodology.
 - It remains unclear when to provide a (future date) Prospective Market Value or when a (current date) Hypothetical Value might suffice, assuming the only difference is the date of value. For example, why are residential subdivisions typically reported as hypothetical values as of the current date yet other proposed construction projects typically warrant prospective values?
- Sales History and Pending Sales
 - Definition states “an appraiser must...analyze” the sales history. However, it remains unclear what is meant by the term “analyze”. This should be better defined as to intent by the regulators, preferably indicating if there is to be comparison of current or historical

information to the current estimate of value – and if a large discrepancy is evident the appraiser must “analyze” (question and justifiably explain) why there is a difference, address the relevance of said difference, and justify why the current value is the most reliable estimate of market value.

- Sum of Retail Sales
 - The term “retail sales” is not well defined and inherently describes “sales” which are committed or consummated transactions. Conversely, the Sum of Retail Sales (formerly called the Sum or Aggregate of Retail Values or Prices) is supposed to be a summation or aggregation of retail prices or price estimates that the individual units might sell for if individually placed on the open market as determined by per-unit appraisals. They are not “sales” and should not be termed as such to avoid potentially misleading the intended user.

Appendix C – Glossary: Undefined Terms Taken from the Guidelines – need to be defined...

- “Higher risk real estate-related financial transactions” (page 13 – Evaluation Content)
 - What constitutes “higher risk”?
- “Portfolio risk increases” (page 13 – Evaluation Content)
 - At what point should increased portfolio risk trigger more detailed evaluation content, and further, when might that signify the need for a full appraisal?
- “Prior approval from primary regulator” (page 14, 38 – Reviewing Appraisals and Evaluations)
 - Refer to prior discussion comments under Reviewing Appraisals and Evaluations.
- “Other low risk mortgage transactions” (page 16, 38 – Request for Comment)
 - Please describe what is specifically meant by this phrase, for clarity.

Appendix C – Glossary: Undefined Terms to be Added to the Guidelines – need to be defined...

- This Glossary should include terms reflective of Workout and OREO situations, especially where the loan is modified as part of an accommodation for risk mitigation or where the loan is fully or partially written-off in foreclosure, bankruptcy, or other non-payoff situation. Regulations change for these situations, yet insufficient term definitions (and instructions or guidelines) are provided to meet these situations.
- Various subdivision appraisal situations demand additional, more descriptive, and unique situation terminology, especially with respect to partially-completed or partially-funded projects that can no longer meet original loan terms or original market supply/demand expectations. Subdivision terminology and guidance have always been scarce, and with the current stressed economy there needs to be more and better defined terms and guidelines.
- Existing terms do not sufficiently reflect adverse or declining life-cycle issues, but rather tend to focus on the more common stable to improving value situations. Regulators may find it useful to expand this Glossary to include the unique terms relevant to various cycle possibilities.

Additional Topic Recommendations to be Covered in Comprehensive Guidelines:

Market Analysis – Not Just Presentation

Market Analysis development and analysis (USPAP Standard 1), and presentation (Standard 2), must be guided to not just present the data but to analyze the impact on the subject property. For example, in the most recent up cycle there were countless land acquisition and/or development loans (A&D) in outlying geographic areas that in normal times would not be considered livable or reasonably commutable to the closest business centers. Another example is the large quantity of “million dollar”

(or high end of price range) condos and/or homes built in any given market. Accurate market analysis would ascertain the potential market share, and market dilution, for such proposed new product based on the quantity and quality of potential buyers and demand for the proposed new product. Analysis should be required to consider “typical” long-range (full cycle) historical demand and not just “current” rapid up-cycle demand if a project is expected to be absorbed in more than 12 months (long-range planning). Too many outlying developments and too many high end homes in a market should trigger a “gag response” toward making a commitment to add to this inventory, or at least accurate and realistic risk-pricing (interest rate, loan term, and/or LTV) to adequately account for the risk of oversupply or the inability to adequately penetrate the market with eventuality of value losses. Appraisers and lenders should be directed to a) require high level feasibility studies for such projects, and b) risk-price accurately to reflect the real risk to the lender regardless of desire to be competitive in the market for new business as the risk of loss may not be able to offset the probability for profit from making the loan (as commonly observed in the current financial market meltdown). Market analysis must be demanded by the lender and provided by the appraiser on these types of higher risk high saturation projects. Assessment must blindly consider the market potential for success regardless of the economy’s current cycle, prior to determining its potential value in the current market economy.

Likewise, top-of-market forecasting must be eliminated. While it may be relevant and supportable in a rapidly growing economic cycle it is rarely sustainable over a holding period as is often projected. Appraisers must take note, and lenders must demand they do note, that market cycles tend to run approximately 10 years. With such information, forecasts should reflect “typical” mid-cycle ranges and not be permitted to reflect any extremes that may be transitory to the immediate cycle snapshot. Aggressive lenders, and borrowers, tend to want to take advantage of top-of-market (and sometimes higher forecast) values and assumptions in strong up-cycles yet these are just the type of short-sighted forecasts that get lenders, appraisers, borrowers, investors, and eventually taxpayers into trouble.

Government Regulatory Agency Consolidation

In light of the mounting federal budget deficit and emphasis on creating efficiencies to effectively minimize (streamline) the size of the federal government, it would seem economically and politically prudent at this time to merge all regulatory agencies into a single regulatory managing entity. The Federal Reserve Board could be the holding or managing entity for all of the regulatory sub-agencies or divisions, with the intent to limit the size of overhead and management as well as to consolidate regulatory policies and procedures (and examiners) wherever feasible and practical to present a single unified interpretation of FRB policy. While thrifts, credit unions, VA, HUD, and other current agencies may wish (and lobby) to continue to operate in support of their disparate constituencies, other than a few unique distinctions these entities are sufficiently similar and should readily be folded into a single regulatory entity managed by the FRB. Politics should NOT play a part in this aggregation and assimilation of regulatory entities, but rather the overriding interests of the taxpaying public should drive this effort.

Separately, now that the GSEs (FNMA and FHLMC) are taxpayer “owned”, it is my contention that they now MUST fall in line with other federally regulated lending institutions and be held to FIRREA and USPAP with no exemptions.

80/20 Rule – Theory vs Reality

It has been the unspoken risk management policy of many, if not all, lenders to put greater due diligence on the 20% of their portfolio that is most likely to represent 80% of the institution’s risk profile. This tacit rule should be dispelled as a realistic approach to risk management by lending institutions. While

any individual loan comprised in the larger 80% considered of lower risk, if the loan decision policy is flawed then the 80/20 Rule becomes flawed and of high risk. For example, any individual subprime ARM loan may not be of substantial risk to the bank as it represents a very minute percentage (miniscule) of the institution's total lending portfolio, however if millions of these loans (substantial percentage of the total lending portfolio) are funded then the inherent risk is aggregated to the point where the loan policy or procedural basis for underwriting these loans may represent high risk to the institution. In the final analysis, the loan is not at risk but rather the loan underwriting policy or procedure presents atypically – and preventably – high risk to the institution. Perhaps some regulatory guide notes should be considered to address the management of such aggregated risk and related loan policies.

Economic Cycle Observation

A final observation...in my experience it always seems that the market will peak when condo construction and conversion become very popular, and when there is rapid growth in licensing of real estate salespeople, appraisers, and mortgage brokers. Perhaps some regulatory "guidance" can be tailored to reflect this cyclical observation? (The nadir of a down cycle is more difficult to assess as recovery tends to move slower than growth and is often accompanied by some type of injected fiscal assistance.)

Thank you for the opportunity to comment on the proposed Guidelines, and for your consideration of my comments and suggestions.

Sincerely,

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