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October 15, 2012

Robert deV. Frierson
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Board of Governors of the Federal Reserve System
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Attention: Comments

Monica Jackson
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National Credit Union Administration
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Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
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Attention: Comments/Legal ESS

Office of the Comptroller of the Currency, Treasury
250 E Street, SW, Mail Stop 2-3
Washington, DC 20219

Re: Proposed Rule of the Board of Governors of the Federal Reserve System, the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the National Credit Union Administration and the Office of the Comptroller of the Currency on Appraisals for Higher-Risk Mortgage Loans Amendments to the Truth in Lending Act (Regulation Z), Docket/RIN Numbers: R-1443/RIN7100-AD90, CFPB-2012-0031/RIN3170- AA11, RIN2590-AA58, RIN3133-AE04, OCC-2012-0013

Ladies and Gentlemen:

Fannie Mae is pleased to submit these comments in response to the proposed rule of the Board of Governors of the Federal Reserve System ("Board"), the Consumer Financial Protection Bureau ("Bureau"), the Federal Deposit Insurance Corporation ("FDIC"), the Federal Housing Finance Agency ("FHFA"), the National Credit Union Administration ("NCUA") and the Office of the Comptroller of the Currency, Treasury ("OCC") on Appraisals for Higher-Risk Mortgage Loans. The Board, the Bureau, the FDIC, the FHFA, the NCUA and the OCC are collectively referred to herein as the "Agencies."

I. Background

The Proposal. The proposal (the "Proposal") implements amendments made by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") to the Truth in Lending Act ("TILA") that (i) define a new category of mortgage loans, higher-risk mortgage loans, and (ii) prohibit creditors from extending credit in the form of higher-risk mortgage loans to consumers unless certain appraisal requirements are met.

Higher-Risk Mortgage Loan Definition. Under the Dodd-Frank Act, a higher-risk mortgage loan is defined as:

- a first lien loan securing the consumer's principal dwelling,
- with an annual percentage rate ("APR") which exceeds the Average Prime Offer Rate ("APOR") for a comparable transaction by 1.5 percentage points, and
- with an original principal amount up to the maximum amount for loans eligible for sale to Fannie Mae or Freddie Mac ("GSEs").[1]

A loan that meets this definition, however, is exempt if it is a qualified mortgage ("QM").[2]

Appraisal Requirements. Before closing a higher-risk mortgage loan, the creditor must obtain a written appraisal of the interior and exterior of the property performed by a certified or licensed appraiser. In addition, if the higher-risk mortgage loan is for the purchase of a property, a second appraisal is required if: (i) the seller acquired the property within 180 days of the consumer's agreement to purchase the property; and (ii) the seller's purchase price was less than the price that the consumer has agreed to pay. The creditor may not charge the consumer for the cost of the second appraisal.

Scope of Comments. Fannie Mae's comments address the following topics:

- *Second Appraisal Requirement Could Have Chilling Effect on Real Estate Owned (REO) Sales* – Fannie Mae is concerned about the potential impact of the Proposal on sales of REO property and neighborhood stabilization efforts. To minimize the potential unintended consequences the proposal might have, we offer possible solutions that would balance the operations of an efficient housing market with the need to protect consumers from excessive real estate speculation;
- *Appraisal Requirements Eliminate a Material Benefit of Streamline Refinance Programs to Consumers* – Fannie Mae requests that the Agencies use their exception authority to exempt conventional streamline refinance loans from the Proposal's appraisal requirements to facilitate consumers moving into less expensive and/or more stable mortgage loans without the cost of an appraisal;
- *Support Harmonization* – Fannie Mae supports the harmonization of this rule with: (i) the Bureau's proposed rule under the Equal Credit Opportunity Act ("ECOA") regarding appraisals or valuations prepared in connection with an application; and (ii) the Bureau's proposed rule under the Home

[1] Also included in the definition of higher-risk loans are: (i) first lien loans securing a consumer's principal dwelling with an original principal amount greater than the GSE maximum if the APR exceeds the APOR by 2.5 percentage points; and (ii) subordinate lien loans secured by the consumer's principal dwelling if the APR exceeds the APOR by 3.5 percentage points.
[2] In addition, the Agencies used exemption authority granted by the Dodd-Frank Act to exclude reverse mortgages and loans secured solely by residential structures (*e.g.*, manufactured housing) from the definition of higher-risk mortgage loans.

Ownership and Equity Protection Act ("HOEPA") regarding use of the transaction coverage rate; and

- *Technical Issue Clarification* – Fannie Mae requests clarification on technical issues relating to documentation to determine sales date and price.

II. Requiring a second appraisal could unintentionally hamper sales of REO and inhibit neighborhood stabilization efforts.

The Proposal. Under the Proposal, a creditor must obtain and pay for a second appraisal if the prior sales transaction was within the previous 180 days and the current sales price is greater than the prior sales price. While the purpose of the provision is to prevent artificially inflated property values and excessive real estate speculation, we see the potential for unintended consequences.

Fannie Mae Comments. When a lender or other owner of a mortgage loan acquires a property through a foreclosure, the transaction is reflected as a sale of the property in the land records. The price at which the foreclosure sale occurs is generally tied to the outstanding principal balance of the loan secured by the foreclosed property which may bear little relation to the property's actual fair market value.

Once Fannie Mae acquires a property, we assess what repairs and improvements are advisable to maximize the REO sales price and minimize losses. Typical improvements made by Fannie Mae include painting, carpeting and new appliances to resell the REO property quickly, minimizing our losses and helping neighborhood stabilization efforts by reducing the inventory of vacant properties.

The majority of the time, however, the property condition or prevailing market conditions indicate that an 'as is' sale is the most appropriate course of action resulting in Fannie Mae selling the property without repairs.[3] These buyers include owner-occupants, private investors, and community non-profits or state or local agencies whose purpose is to promote neighborhood stabilization by rehabilitating and reselling foreclosed properties. In addition to standard negotiated real estate transactions, Fannie Mae may sell REO via single property auctions or through sales of pools of REO properties.

Whether Fannie Mae or a third party repairs or renovates an REO property, it is in everyone's interest to rehabilitate and resell the REO properties to owner-occupants as quickly as possible, both to stabilize neighborhoods and replenish funds to rehabilitate more distressed properties. By way of example, Fannie Mae's goal is to complete the sale of REO properties within 150 days of marketing the property.

A. Potential impact on consumers and investors

Depending on the resale price and whether the purchaser will obtain a higher-risk mortgage loan, the Proposal could have a chilling effect on resales of REO properties repaired by Fannie Mae or rehabilitated by third parties. Sellers generally have no control over what type of loan a consumer will get to finance the purchase of a property. Whether a loan meets the higher-risk threshold depends on both the consumer's credit profile and the creditor's pricing. If the loan for which the consumer would qualify is a higher-risk loan, the creditor could have little incentive to make that loan if the consumer wishes to purchase renovated

[3] Approximately 30% of Fannie Mae REO sold have been repaired and improved and 70% are sold as is. Of the REO that are improved, Fannie Mae spends on average $7,900 per property.

REO property, because the creditor will know that in all likelihood it will have to absorb the cost of the second appraisal, which typically costs between $400 - $600.

If creditors choose to not finance REO sales they may essentially lock-up portions of the credit market for these properties. Alternatively, creditors may refuse to take applications from consumers on REO properties unless the previous sale was significantly older than 180 days, to avoid the need for a second appraisal. This would have the effect of slowing down sales simply to avoid the regulatory requirement, creating an obstacle to the efficient operation of the housing market. Either outcome is problematic in the context of REO sales where ensuring that properties are appropriately rehabilitated and resold quickly is of paramount importance.

Based on Fannie Mae's experience, the Proposal could create a disincentive to investors who want to purchase and rehabilitate distressed properties.[4] If investors believe that they will have to hold the property for a longer period of time to let the regulatory clock run, or that consumers will have difficulty obtaining financing because fewer creditors are willing to lend, investors will be less likely to purchase the property in the first instance, leaving more distressed properties vacant for longer periods of time.[5] In addition, the prospect of longer holding periods may result in investors offering even lower prices to purchase REO properties for rehabilitation, which would further exacerbate our losses.

B. Possible mitigation options (Question 27-29)

There are several ways the Agencies could deal with the unintended consequences that the Proposal has for REO sales, short sales and neighborhood revitalization:

1. *Exempt sales where the improvements to the property support the increased sales price.* The Proposal requires that the second appraisal include an analysis that would support the difference in price between the previous sale and the current sale, including changes in market conditions and any improvements made. Fannie Mae requires a similar analysis, with particular focus on improvements to kitchens and bathrooms, in order for loans to be eligible for sale to us. We require appraisers to identify whether there have been updates or complete renovations and the performance date of such work. If such an analysis were required in connection with the first appraisal, we believe this would alleviate the need (and cost) for the second appraisal. The Agencies could require creditors to adopt similar requirements.

2. *Exempt sales of properties with anti-flipping clauses.* Fannie Mae restricts the resale of REO property and properties approved for short sales for 90 days if the price is in excess of 120% of the price paid to Fannie Mae. This restriction is: (i) reflected in the sales contract and the deed for REO properties; and (ii) required by Fannie Mae's Servicing Guide Announcement SVC-2012-19 for short

[4] Fannie Mae conducted a pilot in the Atlanta area in the mid-2000s. Initially, Fannie Mae adopted a one-year resale prohibition, but soon discovered that the prohibition had a draconian impact on REO sales to investors. Even when Fannie Mae reduced the resale prohibition to 180 days, we found that most investors were still unwilling to purchase REO properties for rehabilitation. As a result, Fannie Mae adopted a 90-day resale prohibition and capped the resale price at 120% over the REO sales price. Fannie Mae adopted the 120% limit based on its on repair costs and expected return on repairs/improvements made as there is not always a dollar-for-dollar correlation between repair dollars spent and the increase in market value.

[5] This may be especially problematic for non-profit entities that participate in the Neighborhood Stabilization Program.

sales. Fannie Mae adopted these measures to prevent flipping of such properties.[6] The Agencies could exempt sales from the second appraisal requirement if, when the seller took title to the property, the seller was subject to an anti-flipping clause as part of its purchase contract and/or deed to the property. For instance, if the clause were to limit the amount that the sales price can increase within 90 days (*e.g.*, up to 120% over the REO sales price), and the price was supported by the first appraisal, then a creditor would not need to obtain a second appraisal.

3. *Exempt sales by non-profits or state/local agencies.* If the property is being sold by a state or local agency or non-profit that is participating in the Neighborhod Stabilization Program, the Agencies could exempt the sale from the second appraisal since there should be no concern about the possibility of artificially inflated property values given the mission of these Neighborhood Stabilization Program participants.

III. Proposal would eliminate material feature of HARP and related streamline refinance programs.

Background. Under the Proposal, higher-risk mortgage loans that satisfy the definition of a QM are not subject to the appraisal rules. Under the Dodd-Frank Act as more fully explained below, conventional streamline refinance programs, such as the Home Affordable Refinance Program (HARP), were not specifically included with government streamline programs offered by the Federal Housing Administration (FHA) or the Department of Veterans Affairs (VA) in terms of QM status. As a result, most conventional streamline refinance loans, including loans refinanced under HARP and Fannie Mae's related Refi Plus program, would not be QM loans under the Dodd-Frank Act. To the extent that such loans fall within the definition of higher-risk mortgage loans,[7] under the Proposal, full appraisals will be required which will eliminate a material benefit to consumers. We request that the Agencies use their exception authority to exempt conventional streamline refinance loans from the Proposal's appraisal requirements in order to facilitate consumers moving into less expensive or more stable mortgage loans without the cost of an appraisal.

QM Status of Government Streamline Refinance Loans. Under the Dodd Frank Act and the proposed QM rule, FHA and VA can establish streamline refinance programs which will be deemed to have satisfied QM requirements. Such authority includes the ability to determine appraisal requirements. For example, FHA's streamline refinance program does not require that an appraisal be conducted and even permits the appraisal to be ignored if the borrower "would be better advised to proceed as if no appraisal had been made."[8]

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[6] See footnote 4.

[7] Depending on loan balance, loan term, the presence of mortgage insurance and whether closing costs are paid for by the lender (*e.g.*, a zero-zero alternative), HARP loans may fall into the higher-risk mortgage loan category because the APR exceeds APOR by more than 1.5%. For example, on September 17, 2012, the average prime offer rates published were 3.60% for 30 year term first lien loans and 2.85% for 15 year term first lien loans. This made the ceiling APR for these products 5.10% and 4.35% respectively at that time. If a borrower does not want to come out-of-pocket to pay closing costs of $2,000, a lender can build these costs into the mortgage rate. Depending on the loan balance and the term of the loan, this impact on the note rate would be much greater for shorter term, lower balance borrowers, than it is for large loan sizes and longer loan terms. The impact of converting $2,000 in closing costs on a 15-year $400,000 loan would require an approximate 0.11% increase in the APR to cover the closing costs; in constrast, a 15-year $25,000 loan would require an approximate 2.67% increase in APR to cover the same closing costs.

[8] HUD Handbook 4155.1.6.C.

No QM Status for Conventional Streamline Refinance Loans. There is no parallel provision in the Dodd-Frank Act for conventional loans[9], and therefore only a very small number of conventional streamline refinances will meet the proposed regulatory definition of a QM unless the Bureau creates a regulatory exemption for conventional streamline refinance loans. As a result, most conventional streamline refinance loans, including loans refinanced under HARP would be required to have full appraisals. This is true notwithstanding the fact that, in order to qualify for a HARP refinancing, the borrower must: (i) be current on the loan; (ii) have no late in payments in the last six months and not more than one late payment in the previous six months; (iii) receive a "benefit" from the transaction in the form of a lower monthly payment of principal and interest, a lower interest rate, a shortened amortization term or movement to a more stable loan product; and (iv) not receive more than a limited amount of cash back from the transaction.[10]

Fannie Mae Request. In Fannie Mae's comment letter concerning the Bureau's QM proposal,[11] we requested that the Bureau use its exception authority to ensure that conventional refinance transactions with similar risk profiles be treated similarly to government programs. If the Bureau takes that step and allows conventional refinancing loans to qualify as QMs, no more needs to be done. If, however, most conventional streamline refinance transactions fall outside of the QM definition,[12] we would request that the Agencies consider exempting conventional streamline refinance transactions, such as HARP refinance loans, from the Proposal's appraisal requirement. The extra time and expense of a full appraisal in these instances is not warranted and could significantly hamper streamline refinancing programs which have been designed to benefit borrowers by placing them in more stable loan products and lowering their payments.[13]

IV. Regulatory provisions should be harmonized whenever possible: Questions 6-9 and Question 42.

In a separate rulemaking, the Bureau has proposed to make the finance charge under TILA more inclusive by adding in fees that are currently excluded. The result of this would be to increase the APR, which would

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[9] Notwithstanding the lack of statutory language, there is evidence in the legislative history that lawmakers wished to extend similar discretion with respect to conventional streamline refinance programs. In a colloquy, Senator Dodd stated:

> However, certain refinance loans, such as VA-guaranteed mortgages refinanced under the VA Interest Rate Reduction Loan Program or the FHA streamlined refinance program, which are rate-term refinance loans and are not cash-out refinances, may be made without fully reunderwriting the borrower, subject to certain protections laid out in the legislation, while still remaining qualified mortgages.
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> *It is the conferees' intent that the Federal Reserve Board and the CFPB use their rulemaking authority under the enumerated consumer statutes and this legislation to extend this same benefit for conventional streamlined refinance programs where the party making the new loan already owns the credit risk. This will enable current homeowners to take advantage of current low interest rates to refinance their mortgages.*

156 Cong. Rec. 5928 (July 15, 2010).

[10] Fannie Mae currently limits cash back to the nominal amount of $250.
[11] Fannie Mae Comment Letter to the Bureau of Consumer Financial Protection, Docket No. R-1417 (Regulation Z, Truth in Lending), submitted July 22, 2011.
[12] See footnote 7.
[13] The HARP program is currently set to expire December 31, 2013, however, the Proposal could become effective before that date and/or the HARP program could be extended or another program put in place.

affect the number of loans covered by this and other rules. To off-set this impact, the Bureau is proposing to use a new transaction coverage rate ("TCR") so that the number of loans covered remains approximately the same if the more inclusive finance charge is adopted. In this Proposal, the Agencies are seeking comment on this approach and the use of the TCR if the more inclusive finance charge is adopted. We supported this approach in the HOEPA Proposal, including the mandatory use of the TCR if it is adopted, and restate our support here.

A. Harmonization with proposed ECOA appraisal disclosure: Question 42

Both this Proposal and a proposed appraisal rule under the Equal Credit Opportunity Act (ECOA) require that applicants be provided with notices regarding appraisals or valuations prepared in connection with a credit application. Although both proposed rules are the result of amendments made by the Dodd-Frank Act, the language in the two notices differs. The Bureau proposes to harmonize the language in a way that will satisfy both requirements and eliminate any need for a creditor to provide two different notices. We support this harmonization. We request that the Bureau refer to valuations as well as appraisals in the proposed disclosure, so that applicants understand that some of the information they may be receiving is not an appraisal and was not developed by a state-licensed or certified appraiser. This will help prevent borrowers coming to the mistaken conclusion that Fannie Mae is an appraiser or appraisal management company.

V. Creditors should be allowed to rely on a variety of documents to determine prior sales date and price: Question 35.

Creditors Should be Allowed to Rely on Current Appraisal for Prior Sales Data. The Proposal lists several different documents that a creditor could use to determine the sales price for the property in the preceding transaction. The agencies specifically request comment on whether creditors should also be permitted to use the appraisal conducted in connection with the consumer's transaction to determine the prior sales price and date. Fannie Mae supports the use of the documents listed in the Proposal and further agrees that it is appropriate to allow creditors to use the current appraisal. Given the time delays that occur with the recording of sales and lag time for tax assessments, not to mention the data limitations for non-disclosure jurisdictions, the best source of data may be from multiple listing services which are captured in the appraisal.

The Agencies Should Provide Guidance on Which Value a Creditor Can Use When It Has Multiple Documents Reflecting Different Values. While the creditor may have difficulty documenting the previous sales price in some instances, the reverse is also likely to be true – the creditor may find that it has multiple documents reflecting the prior sales price, but the documents themselves may each state different values, including a multiple listing service value, a tax records value and possibly a prior appraisal. We request that the Agencies clarify that when the creditor has multiple documents, each reflecting a different value for the prior sale, the creditor is in compliance with the regulation if it chooses to use any one of those values.

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We appreciate the opportunity to provide the foregoing comments to the Agencies on higher-risk mortgage loans and associated appraisal requirements for such loans. If you have questions regarding the matters addressed in this letter, please feel free to contact Sheila Teimourian at Sheila_Teimourian@FannieMae.com or Sheilah Goodman at Sheilah_Goodman@FannieMae.com.

Sincerely,

Sheila Teimourian
VP and Deputy General Counsel