

Real Estate Valuation Advocacy Association

Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090
Attn: Ms. Elizabeth M. Murphy, Secretary

November 15, 2010

Re: File Number S7-26-10: Issuer Review of Assets in Offerings of Asset-Backed Securities

The Real Estate Valuation Advocacy Association (“REVAA”)¹ is pleased to offer its comments on the proposed rulemaking by the Securities and Exchange Commission (the “Commission”) to implement Section 945 and a portion of Section 932 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Act”). REVAA supports the Commission’s efforts to provide investors with appropriate transparency for the securitization due diligence process. Further, we believe that the real estate valuation products offered by REVAA member companies provide important data for consideration by issuers, ratings agencies and their authorized agents in residential mortgage-backed securities (“RMBS”) offerings.

Need for Limited Definition of Third Party Due Diligence Providers

In our view the proposed rulemaking requires greater clarity and specificity on the specialized industry of “third-party due diligence providers” that have historically assisted issuers with their underwriting analysis and the assessment of pool risks. As you are aware, the proposed rulemaking would require that such due diligence providers (i) consent to being named as experts in the registration statement for registered asset-backed securities transactions, and (ii) have their findings and conclusions disclosed in filings under the Securities Exchange Act of 1934. While the Commission suggests that “a *third party engaged for the purposes of performing a review* is a broad category that would include any third party on which the issuer relies to review assets in the pool,” REVAA believes that the assumptions underlying the proposed rulemaking actually point to a much more limited group of intended third party providers that would be subject to the rulemaking’s requirements.² The broader definition suggested by the Commission would have unintended negative consequences for the real estate valuation process, which in many instances could be contrary to the interests of investors.

For example, while REVAA member companies may provide issuers and their agents with appraisals and alternative valuation reports on the real estate held as collateral for a pool of loans in an RMBS transaction, these products do not in and of themselves provide an analysis or assessment of a particular property’s (let alone a particular loan’s) suitability for inclusion in the RMBS pool. Rather, these valuation

¹ REVAA is a trade association with member companies dedicated to the maintenance and further development of high quality standards within the real estate valuation industry and the advocacy of related causes. REVAA promotes high ethical standards, political awareness, and the growth of the real estate valuation industry as a whole. REVAA is comprised of companies that produce and sell, or benefit from, real estate valuation products including Appraisals, Broker Price Opinions (BPOs), Automated Valuation Models (AVMs) and other innovative valuation approaches that benefit mortgage investors, servicers, originators and borrowers.

² Note, for example, that the “specialized industry of third-party due diligence firms” referenced on page 9 of the proposed rulemaking refers to testimony describing a fairly limited category of companies that provide issuers with underwriting analysis and risk management services related to the inclusion of pool assets in an RMBS transaction. See Testimony of Vicki Beal, Senior Vice President Clayton Holdings, Before the Financial Crisis Inquiry Commission (Sept. 23, 2010), available at <http://www.fcic.gov/hearings/pdfs/2010-0923-Beal.pdf>. Likewise, other cited sources in the proposed rulemaking and in Commissioner remarks also discuss “due diligence firms” in this more specialized context. See Vikas Bajaj and Jenny Anderson, Inquiry Focuses on Withholding of Data on Loans, N.Y. TIMES, January 12, 2008; E. Scott Reckard, Sub-prime Mortgage Watchdogs Kept on Leash: Loan Checkers Say Their Warnings of Risk Were Met with Indifference, LOS ANGELES TIMES, March 17, 2008, at C1; Enhancing Investor Protection and the Regulation of Securities Markets—Part I: Testimony before the U.S. Senate Committee on Banking, Housing, and Urban Affairs, 111th Congress, 1st session, p.55 (2009) (Testimony of Professor John Coffee).

reports simply provide objective data to issuers and/or their outsourced due diligence agents to use in their due diligence review and analysis of an RMBS transaction, much the same as a credit bureau might provide credit scores for borrowers on the loans in an RMBS asset pool. Further, these valuation reports do not directly relate to pool assets, they merely provide valuation information on the real property that serves as collateral for the pool's loan assets. Typically, individual property valuations merely provide one data point to the broader analysis of the overall assets included in a loan pool.

Therefore, REVAA urges that proposed Rule 193 of the Securities Act of 1933 and proposed Rule 15Ga-2 of the Securities Exchange Act of 1934 be revised, at the very least, to clarify that the term "third-party due diligence providers" would not include third parties such as real estate valuation providers who merely provide data or reports for the issuer's consideration as part of its due diligence review. REVAA notes that there may be an unforeseen chilling effect on the availability of independent third party due diligence services even where the proposed rulemaking is limited to traditional third party due diligence providers. However, we have chosen to limit our commentary solely to the rulemaking's potential impact on the real estate valuation community and RMBS transactions.

Consequences of Expert Status for Providers of Real Estate Valuation Products

Requiring that valuation companies, appraisers and/or other real estate professionals providing valuation products be named as experts in a registration statement for an RMBS offering would result in negative unintended consequences. REVAA believes that issuers, underwriters, investors, and ratings agencies all benefit from a free flow of information on which to base their due diligence analysis. If the mere delivery of real estate valuation information to an issuer or its agent would result in a valuation company, appraiser or real estate professional being subject, potentially, to expert liability to RMBS investors and others, many of these providers would limit access to their valuation products for such purposes to avoid the unintended liability that could result from the use, or misuse, of their products. This could in fact result in a decrease in the available due diligence data to support an analysis of a loan pool.

This concern is even more pronounced for individual appraisers and real estate professionals, who often provide their valuation reports through valuation management companies and thus are far removed from the actual securitization process. Appraisers in particular are subject to numerous requirements under the Uniform Standards of Professional Appraisal Practice ("USPAP") to appropriately define the scope of work required for an appraisal assignment as well as the intended use and intended users of the appraisal report.³ Appraisal reports in RMBS transactions are typically provided to the issuer or a third party due diligence provider to assist them in their evaluation of property values. Treating such an appraiser as an expert in the registration statement with potential liability to RMBS investors fundamentally transforms the appraiser's role and responsibilities. Expert status might be warranted where the specific property or other asset being appraised is a material asset in a registered offering and the appraiser is engaged with full knowledge of the appraisal's intended use (allowing the appraiser to define an appropriate scope of work and fee for the assignment), but it would be excessive in most RMBS transactions where the property itself is not a pool asset but rather serves as collateral for one of many loans involved in the offering.⁴ Each individual property is typically a small fraction of the overall collateral supporting an RMBS transaction.

Further, the proposed rulemaking does not provide sufficient guidance on the information that a valuation company, appraiser or real estate professional would certify as an expert. If valuation providers were named as experts with respect to valuation opinions for specific properties disclosed in the registration statement, the resulting liability exposure to RMBS investors would be entirely out of proportion to the

³ See Scope of Work Rule and Standards Rule 1-2 in the Uniform Standards of Professional Appraisal Practice.

⁴ While Section 11(a)(4) of the Securities Act of 1933 provides for "expert" liability for "every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him" [**emphasis added**], this liability only applies where the individual is named as having prepared or certified any report or valuation which is used in connection with the registration statement. In the absence of a requirement under the proposed rulemaking that appraisers must be treated as "third party due diligence providers," we believe that an appraiser who provides an issuer or its agents with an appraisal report on a property collateralizing a loan in an RMBS pool would typically not be named in the registration statement and therefore would not incur expert liability.

fees currently earned for such services. This would cause valuation providers to either refrain from offering valuation services for registered RMBS transactions or to charge significantly higher fees (in which case issuers would most likely reduce the sample size of properties for which they seek valuations). In either case, issuers would have less information at their disposal to aid in their due diligence review. Further, given the large number of separate valuation providers involved in reviewing the collateral underlying the typical loan portfolio, such an arrangement is also highly impractical.

It would also be inappropriate to require valuation providers to be named as experts with respect to a more limited disclosure such as the steps that were followed to value properties in an RMBS transaction (for example, the sample size of properties evaluated and the type of valuation performed). These procedures are dictated by the issuer rather than the valuation provider. The valuation provider does not exercise any independent professional judgment in defining this process, but merely delivers the valuations that are requested by the issuer. Therefore, with respect to the development of collateral valuation procedures in an RMBS transaction, the valuation provider is not acting in a capacity that would typically be deemed to require expert status under Section 11(a)(4) of the Securities Act of 1933.⁵

Importance of Alternative Valuation Products in the Securitization Process

The Commission also elicits comments on whether there should be a minimum scope of review that issuers must perform in RMBS or other asset-backed securities transactions. While REVAA does not believe that real estate valuation companies, appraisers and other real estate professionals should be deemed to be “third party due diligence providers” that are subject to the rulemaking’s requirements for expert status and Exchange Act disclosure, such parties nonetheless play an important role in the overall RMBS securitization process by providing issuers and third party due diligence providers with the data necessary to perform appropriate due diligence reviews. In this regard, REVAA strongly believes that the free flow of real estate valuation information is integral to ensuring that issuers have the appropriate tools at their disposal to fully understand the value of the real estate securing the loan assets in an RMBS transaction, and to make informed risk management decisions. Therefore, any minimum review standards must be cognizant of an issuer’s need for flexibility and multiple data sources to design appropriate methodologies to analyze collateral valuation.⁶

For example, issuers may choose to apply a waterfall methodology that enables them to examine the values of a wide range of properties in differing manners based on perceived risks. In such a scenario, the issuer may initially test the current values of a large sample of properties using an automated valuation model (“AVM”) or other automated valuation tool to provide a first glimpse into the value characteristics of the real property securing the loans in an asset pool. Where the AVM identifies property values that show an excessive variance from the values indicated in the loan files, a broker price opinion (“BPO”) performed by a real estate broker or agent may be ordered to provide a deeper dive into the property’s value. Finally, for the reduced subset of loans that continue to demonstrate collateral valuation issues, the issuer may order a more extensive and costly appraisal product performed by a licensed or certified appraiser. By utilizing a waterfall approach, the issuer is able to economically and efficiently analyze a large sample of properties, while allocating more time and money to those properties whose values are identified as being higher risk.

The importance of providing issuers with the opportunity to use multiple data points to assist them in performing their due diligence analysis in RMBS transactions cannot be understated. REVAA believes that any standards developed to review the accuracy of property values reported by originators must be sufficiently flexible to allow issuers continued access to a wide range of valuation tools.

⁵ In this regard it is also unclear how a valuation management company, which typically obtains a valuation report from an appraiser or real estate professional and then provides it to the issuer, would be deemed in any context to be exercising the “professional judgment” normally attributed to experts under the securities laws.

⁶ In this regard we note the Commission’s May 3, 2010 proposed rules on asset-backed securities (File No. S7-08-10) that would require issuers to disclose specific data relating to the terms and underwriting characteristics for each loan or asset in an asset pool. Under the proposed rules, appraisals, BPOs, AVMs and indexes are all appropriate tools for determining the value of real estate securing mortgage loans.

Conflicts of Interest

The Commission further requests comment on whether third parties providing services to issuers are potentially subject to the same conflicts of interest present in the “issuer pays” model that applies to credit ratings agencies. In this regard REVAAs notes that the Board of Governors of the Federal Reserve System recently released an Interim Final Rule implementing Section 129E of the Truth in Lending Act, as required by Section 1472 of the Act. In part, Section 129E imposes stringent independence standards on appraisers and real estate professionals providing BPOs in consumer credit transactions secured by a consumer’s principal dwelling. While Section 129E would not directly apply to valuations ordered as part of an RMBS transaction, REVAAs notes that the real estate valuation industry has taken significant steps toward applying these same independence protections for all uses of appraisals and BPOs in today’s mortgage lending industry.

REVAAs appreciates the opportunity to provide our comments on the role that real estate valuations play in issuer due diligence reviews for RMBS transactions. We stand ready to assist your ongoing efforts in any way we can. Please don’t hesitate to contact us with any further questions you may have, or if you wish to discuss any of our input further.

Sincerely,

Donald E. Kelly, Executive Director

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