

**DEPARTMENT OF THE TREASURY**

**Office of the Comptroller of the Currency**

**[12 CFR Part 34]**

**[Docket No. OCC-2017-0011]**

**[RIN 1557-AE18]**

**FEDERAL RESERVE SYSTEM**

**[12 CFR Part 225]**

**[Docket No. ]**

**[RIN ]**

**FEDERAL DEPOSIT INSURANCE CORPORATION**

**[12 CFR Part 323]**

**[RIN 3064-AE56]**

**Billing Code: 6714-01-P**

**Real Estate Appraisals**

**AGENCIES:** Office of the Comptroller of the Currency, Treasury (OCC); Board of Governors of the Federal Reserve System (Board); and Federal Deposit Insurance Corporation (FDIC).

**ACTION:** Notice of proposed rulemaking and request for comment.

**SUMMARY:** The OCC, Board, and FDIC (collectively, the agencies) are inviting comment on a proposed rule to amend the agencies' regulations requiring appraisals of real estate for certain transactions. The proposal would increase the threshold level at or below which appraisals would not be required for commercial real estate transactions from \$250,000 to \$400,000. This proposed change to the appraisal threshold reflects comments the agencies received through the regulatory review process required by the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA) and completed in early 2017. For commercial real estate transactions

with a value at or below the proposed threshold, the amended rule would require institutions to obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices if the institution does not obtain an appraisal by a state certified or licensed appraiser.

**DATES:** Comments must be received by [INSERT DATE 60 DAYS FROM PUBLICATION IN THE FEDERAL REGISTER]

**ADDRESSES:** Interested parties are encouraged to submit written comments jointly to all of the agencies. Commenters should use the title “Real Estate Appraisals” to facilitate the organization and distribution of comments among the agencies. Interested parties are invited to submit written comments to:

**Office of the Comptroller of the Currency:** Because paper mail in the Washington, DC area and at the OCC is subject to delay, commenters are encouraged to submit comments by the Federal eRulemaking Portal or e-mail, if possible. Please use the title “Real Estate Appraisals” to facilitate the organization and distribution of the comments. You may submit comments by any of the following methods:

- Federal eRulemaking Portal—Regulations.gov: Go to [www.regulations.gov](http://www.regulations.gov). Enter ["Docket ID OCC-2017-0011"] in the Search Box and click "Search." Click on “Comment Now” to submit public comments.
- Click on the “Help” tab on the Regulations.gov home page to get information on using Regulations.gov, including instructions for submitting public comments.
- E-mail: [regs.comments@occ.treas.gov](mailto:regs.comments@occ.treas.gov).
- Mail: Legislative and Regulatory Activities Division, Office of the Comptroller of the Currency, 400 7<sup>th</sup> Street, SW., Suite 3E-218, Mail Stop 9W-11, Washington, DC 20219.

- Fax: (571) 465-4326.
- Hand Delivery/Courier: 400 7<sup>th</sup> Street, SW., Suite 3E-218, Mail Stop 9W-11, Washington, DC 20219.

*Instructions*: You must include “OCC” as the agency name and [“Docket ID OCC- 2017-0011”] in your comment. In general, OCC will enter all comments received into the docket and publish them on the Regulations.gov website without change, including any business or personal information that you provide such as name and address information, e-mail addresses, or phone numbers. Comments received, including attachments and other supporting materials, are part of the public record and subject to public disclosure. Do not enclose any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.

You may review comments and other related materials that pertain to this proposed rule by any of the following methods:

- Viewing Comments Electronically: Go to [www.regulations.gov](http://www.regulations.gov). Enter [“Docket ID OCC-2017-0011”] in the Search box and click "Search." Click on “Open Docket Folder” on the right side of the screen and then “Comments.” Comments can be filtered by clicking on “View All” and then using the filtering tools on the left side of the screen.
- Click on the “Help” tab on the Regulations.gov home page to get information on using Regulations.gov. Supporting materials may be viewed by clicking on “Open Docket Folder” and then clicking on “Supporting Documents.” The docket may be viewed after the close of the comment period in the same manner as during the comment period.

- Viewing Comments Personally: You may personally inspect and photocopy comments at the OCC, 400 7<sup>th</sup> Street, SW., Washington, DC. For security reasons, the OCC requires that visitors make an appointment to inspect comments. You may do so by calling (202) 649-6700 or, for persons who are deaf or hard of hearing, TTY, (202) 649-5597. Upon arrival, visitors will be required to present valid government-issued photo identification and to submit to security screening in order to inspect and photocopy comments.

**Board of Governors of the Federal Reserve System:** You may submit comments, identified by [Docket No. XXXX and RIN No. XXXX], by any of the following methods:

- Agency website: <http://www.federalreserve.gov>. Follow the instructions for submitting comments at <http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm>.
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- E-mail: [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov). Include the docket number and RIN number in the subject line of the message.
- Fax: (202) 452-3819 or (202) 452-3102.
- Mail: Address to Ann E. Misback, Secretary, Board of Governors of the Federal Reserve System, 20<sup>th</sup> Street and Constitution Avenue, NW., Washington, DC 20551.

All public comments will be made available on the Board's Web site at

<http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm> as submitted, unless modified for technical reasons. Accordingly, comments will not be edited to remove any identifying or contact information. Public comments may also be viewed electronically or in paper form in

Room 3515, 1801 K Street, NW. (between 18<sup>th</sup> and 19<sup>th</sup> Streets NW.), Washington, DC 20006  
between 9:00 a.m. and 5:00 p.m. on weekdays.

**Federal Deposit Insurance Corporation:** You may submit comments, identified by RIN 3064-AE56, by any of the following methods:

- **Federal eRulemaking Portal:** <http://www.regulations.gov>. Follow the instructions for submitting comments.
- **Agency website:** <http://www.FDIC.gov/regulations/laws/federal/propose.html>.
- **Mail:** Robert E. Feldman, Executive Secretary, Attention: Comments/Legal ESS, Federal Deposit Insurance Corporation, 550 17<sup>th</sup> Street, NW., Washington, DC 20429.
- **Hand Delivered/Courier:** The guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7:00 a.m. and 5:00 p.m.
- **E-mail:** [Comments@FDIC.gov](mailto:Comments@FDIC.gov). Comments submitted must include “FDIC” and “Real Estate Appraisals.” Comments received will be posted without change to <http://www.fdic.gov/regulations/laws/federal/propose.html> including any personal information provided.

**FOR FURTHER INFORMATION CONTACT:**

**OCC:** G. Kevin Lawton, Appraiser (Real Estate Specialist), (202) 649-7152, Mitchell E. Plave, Special Counsel, Legislative and Regulatory Activities Division, (202) 649-5490, for persons who are deaf or hard of hearing, TTY, (202) 649-5597, or Christopher Manthey, Special Counsel, or Joanne Phillips, Attorney, Bank Activities and Structure Division, (202) 649-5500, Office of the Comptroller of the Currency, 400 7<sup>th</sup> Street, SW., Washington, DC 20219.

**Board:** Anna Lee Hewko, Associate Director, (202) 530-6260, or Carmen Holly, Senior Supervisory Financial Analyst, (202) 973-6122, Division of Supervision and Regulation; or Gillian Burgess, Senior Counsel, (202) 736-5564, Matthew Suntag, Senior Attorney, (202) 452-3694, or Kirin Walsh, Attorney, (202) 452-3058, Legal Division, Board of Governors of the Federal Reserve System, 20<sup>th</sup> and C Streets NW., Washington, DC 20551.

**FDIC:** Beverlea S. Gardner, Senior Examination Specialist, Division of Risk Management and Supervision, at (202) 898-3640, Mark Mellon, Counsel, Legal Division, at (202) 898-3884, Kimberly Stock, Counsel, Legal Division, at (202) 898-3815, Benjamin K. Gibbs, Counsel, at (202) 898-6726, or Lauren Whitaker, Senior Attorney, at (202) 898-3872, Federal Deposit Insurance Corporation, 550 17th Street, NW., Washington, DC 20429.

#### **SUPPLEMENTARY INFORMATION:**

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## **I. INTRODUCTION**

### ***A. Background***

Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (Title XI)<sup>1</sup> directs each Federal financial institutions regulatory agency<sup>2</sup> to publish appraisal regulations for federally related transactions within its jurisdiction. The purpose of Title XI is to protect federal financial and public policy interests<sup>3</sup> in real estate-related transactions by

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<sup>1</sup> 12 U.S.C. 3331 *et seq.*

<sup>2</sup> “Federal financial institutions regulatory agency” means the Board, the FDIC, the OCC, the NCUA, and, formerly, the Office of Thrift Supervision. 12 U.S.C. 3350(6).

<sup>3</sup> These interests include those stemming from the federal government’s roles as regulator and deposit insurer of financial institutions that engage in real estate lending and investment, guarantor or lender on mortgage loans, and as a direct party in real-estate related financial

requiring that real estate appraisals used in connection with federally related transactions (Title XI appraisals) be performed in accordance with uniform standards, by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision.<sup>4</sup>

Title XI directs the agencies to prescribe appropriate standards for Title XI appraisals under the agencies' respective jurisdictions,<sup>5</sup> including, at a minimum, that Title XI appraisals be: (1) performed in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP);<sup>6</sup> (2) written appraisals, as defined by the statute; and (3) subject to appropriate review for compliance with USPAP. All federally related transactions must have Title XI appraisals.

Title XI defines a "federally related transaction" as a real estate-related financial transaction that is regulated or engaged in by a federal financial institutions regulatory agency and requires the services of an appraiser.<sup>7</sup> A real estate-related financial transaction is defined as any transaction that involves: (i) the sale, lease, purchase, investment in or exchange of real

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transactions. These federal financial and public policy interests have been described in predecessor legislation and accompanying Congressional reports. See Real Estate Appraisal Reform Act of 1988, H.R. Rep. No. 100-1001, pt. 1, at 19 (1988); 133 Cong. Rec. 33047-33048 (1987).

<sup>4</sup> 12 U.S.C. 3331.

<sup>5</sup> 12 U.S.C. 3339. The agencies' Title XI appraisal regulations apply to transactions entered into by the agencies or by institutions regulated by the agencies that are depository institutions or bank holding companies or subsidiaries of depository institutions or bank holding companies. OCC: 12 CFR 34, subpart C; Board: 12 CFR 225.61(b); 12 CFR Part 208, Subpart E; FDIC: 12 CFR Part 323.

<sup>6</sup> USPAP is written and interpreted by the Appraisal Standards Board of the Appraisal Foundation. Adopted by Congress in 1989, USPAP contains generally recognized ethical and performance standards for the appraisal profession in the United States, including real estate, personal property, and business appraisals. See [http://www.appraisalfoundation.org/imis/TAF/Standards/Appraisal\\_Standards/Uniform\\_Standards\\_of\\_Professional\\_Appraisal\\_Practice/TAF/USPAP.aspx?hkey=a6420a67-dbfa-41b3-9878-fac35923d2af](http://www.appraisalfoundation.org/imis/TAF/Standards/Appraisal_Standards/Uniform_Standards_of_Professional_Appraisal_Practice/TAF/USPAP.aspx?hkey=a6420a67-dbfa-41b3-9878-fac35923d2af).

<sup>7</sup> 12 U.S.C. 3350(4) (defining "federally related transaction").

property, including interests in property, or financing thereof; (ii) the refinancing of real property or interests in real property; and (iii) the use of real property or interests in real property as security for a loan or investment, including mortgage-backed securities.<sup>8</sup>

The agencies have authority to determine those real estate-related financial transactions that do not require the services of a certified or licensed appraiser and are therefore exempt from the appraisal requirements of Title XI. These real estate-related financial transactions are not federally related transactions under the statutory or regulatory definitions because they are not required to have Title XI appraisals.<sup>9</sup>

The agencies have exercised this authority by exempting several categories of real estate-related financial transactions from the appraisal requirements.<sup>10</sup> The agencies have determined that these categories of transactions do not require appraisals by state certified or licensed appraisers in order to protect federal financial and public policy interests or to satisfy principles of safe and sound banking.

In 1992, Congress amended Title XI, expressly authorizing the agencies to establish a threshold level at or below which an appraisal by a state certified or licensed appraiser is not required in connection with federally related transactions if the agencies determine in writing that the threshold does not represent a threat to the safety and soundness of financial institutions.<sup>11</sup> In the Dodd Frank Wall Street Reform and Consumer Protection Act (the Dodd-

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<sup>8</sup> 12 U.S.C. 3350(5).

<sup>9</sup> See 59 FR 29482 (June 7, 1994)

<sup>10</sup> See OCC: 12 CFR 34.43(a); Board: 12 CFR 225.63(a); FDIC: 12 CFR 323.3(a).

<sup>11</sup> Housing and Community Development Act of 1992, Pub. L. No. 102-550, § 954, 106 Stat. 3894 (amending 12 U.S.C. 3341).

Frank Act),<sup>12</sup> Congress amended the threshold provision to require concurrence “from the Bureau of Consumer Financial Protection that such threshold level provides reasonable protection for consumers who purchase 1—4 unit single-family residences.”<sup>13</sup> As noted above, transactions at or below the threshold level are exempt from the Title XI appraisal requirements and thus are not federally related transactions.

Under the current thresholds, which were established by rulemaking in 1994,<sup>14</sup> all real estate-related financial transactions with a transaction value<sup>15</sup> of \$250,000 or less, as well as certain real estate-secured business loans (qualifying business loans) with a transaction value of \$1 million or less, do not require appraisals.<sup>16</sup> Qualifying business loans are business loans that are real estate-related financial transactions and that are not dependent on the sale of, or rental income derived from, real estate as the primary source of repayment.<sup>17</sup>

For real estate-related financial transactions that are exempt from the appraisal requirement because they are within the applicable thresholds or qualify for the exemption for certain existing extensions of credit,<sup>18</sup> the appraisal regulations require financial institutions to

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<sup>12</sup> Pub. L. No. 111–203, 124 Stat.1376.

<sup>13</sup> Dodd-Frank Act, § 1473, 124 Stat. 2190 (amending 12 U.S.C. 3341(b)).

<sup>14</sup> See 59 FR 29482 (June 7, 1994). The NCUA promulgated a similar rule with similar thresholds in 1995. 60 FR 51889 (October 4, 1995).

<sup>15</sup> For loans and extensions of credit, the transaction value is the amount of the loan or extension of credit. For sales, leases, purchases, investments in or exchanges of real property, the transaction value is the market value of the real property. For the pooling of loans or interests in real property for resale or purchase, the transaction value is the amount of each such loan or the market value of each such real property, respectively. See OCC: 12 CFR 34.42(m); Board: 12 CFR 225.62(m); FDIC: CFR 323.2(m).

<sup>16</sup> See OCC: 12 CFR 34.43(a)(1) and (5); Board: 12 CFR 225.63(a)(1) and (5); FDIC: 12 CFR 323.3(a)(1) and (5).

<sup>17</sup> OCC: 12 CFR 34.43(a)(5); Board: 12 CFR 225.63(a)(5); FDIC: 12 CFR 323.3(a)(5).

<sup>18</sup> Transactions that involve an existing extension of credit at the lending institution are exempt from the Title XI appraisal requirements, but are required to have evaluations, provided that there has been no obvious and material change in market conditions or physical aspects of the

obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices.<sup>19</sup> An evaluation should contain sufficient information and analysis to support the financial institution's decision to engage in the transaction. However, evaluations need not be performed in accordance with USPAP or by certified or licensed appraisers. The agencies have provided supervisory guidance for conducting evaluations in a safe and sound manner in the *Interagency Appraisal and Evaluation Guidelines* (Guidelines).<sup>20</sup>

### ***B. The EGRPRA Process***

In early 2017, the agencies completed a review of their regulations pursuant to EGRPRA, which requires that, not less than once every 10 years, the Federal Financial Institutions Examination Council (FFIEC), Board, OCC, and FDIC conduct a review of their regulations to identify outdated or otherwise unnecessary regulatory requirements imposed on insured depository institutions (IDIs).<sup>21</sup>

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property that threatens the adequacy of the institution's real estate collateral protection after the transaction, even with the advancement of new monies; or there is no advancement of new monies, other than funds necessary to cover reasonable closing costs. See OCC: 12 CFR 34.43(a)(7) and (b); Board: 12 CFR 225.63(a)(7) and (b); FDIC: 12 CFR 323.3(a)(7) and (b).

<sup>19</sup> See OCC: 12 CFR 34.43(b); Board: 12 CFR 225.63(b); FDIC: 12 CFR 323.3(b).

<sup>20</sup> 75 FR 77450 (Dec. 10, 2010). See also Interagency Advisory on the Use of Evaluations in Real-Estate Related Financial Transactions, OCC Bulletin 2016-8 (March 4, 2016); Board SR Letter 16-5 (March 4, 2016); Supervisory Expectations for Evaluations, FDIC FIL-16-2016 (March 4, 2016).

<sup>21</sup> Pub. L. No. 104-208, Div. A, Title II, § 2222, 110 Stat. 3009-414, (1996) (codified at 12 U.S.C 3311). The FFIEC is an interagency body comprised of the Board, OCC, FDIC, NCUA, Bureau of Consumer Financial Protection (CFPB) and State Liaison Committee. Of these, only the Board, OCC and FDIC are statutorily required to undertake the EGRPRA review. The FFIEC does not issue regulations that impose burden on financial institutions and therefore its regulations were not included in the EGRPRA review. The NCUA is not required to participate in the EGRPRA review, but elected to review its regulations pursuant to the goals of EGRPRA, as it did during the agencies' first EGRPRA review 10 years ago. Accordingly, the NCUA participated in the recent EGRPRA review process with the Board, OCC and FDIC. The results of the NCUA's review are included in Part II of the EGRPRA Report, described below. The

As part of the EGRPRA review, the agencies received numerous comments from bankers, banking trade associations, associations of appraisers, and other commenters related to the Title XI appraisal regulations. These comments included recommendations to increase the thresholds at or below which real estate-related financial transactions are exempt from the Title XI appraisal requirements. Some commenters noted that the current thresholds have not been adjusted since they were established in 1994, even though property values have increased, and that the time and cost associated with the appraisal process impose an unnecessary burden in the completion of smaller-dollar amount real estate-related transactions. Some commenters also argued that the time and financial costs attributed to meeting the appraisal requirements at the current threshold levels particularly affect banks in rural markets. These commenters contended that it is often difficult to find state certified and licensed appraisers to complete assignments for properties in rural areas.<sup>22</sup>

In March 2017, the agencies submitted a joint EGRPRA report to Congress (EGRPRA Report) that identified potential initiatives to reduce regulatory burden.<sup>23</sup> In the EGRPRA Report, the agencies addressed comments received concerning the appraisal thresholds and stated that the agencies would propose an increase to the threshold for commercial real estate

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CFPB is required to review its significant rules and publish a report of its review no later than five years after the rules takes effect. See 12 U.S.C. 5512(d).

<sup>22</sup> Earlier this year, the agencies and the NCUA issued an advisory on appraiser availability that points to alternatives that may help in areas facing a shortage of appraisers. *Interagency Advisory on the Availability of Appraisers*. See OCC Bulletin 2017-19 (May 31, 2017); Board SR Letter 17-4 (May 31, 2017); FDIC FIL-19-2017 (May 31, 2017).

<sup>23</sup> FFIEC, *Joint Report to Congress: Economic Growth and Regulatory Paperwork Reduction Act*, (March 2017), (EGRPRA Report), *available at* [https://www.ffiec.gov/pdf/2017\\_FFIEC\\_EGRPRA\\_Joint-Report\\_to\\_Congress.pdf](https://www.ffiec.gov/pdf/2017_FFIEC_EGRPRA_Joint-Report_to_Congress.pdf).

transactions from \$250,000 to \$400,000.<sup>24</sup> Section II of this **Supplementary Information** invites comments on this proposed increase. The agencies also stated their intention to gather more information about the appropriateness of increasing the \$1 million threshold for qualifying business loans, which is being done through a request for comment in Section III of the **Supplementary Information**.

In the EGRPRA Report, the agencies also addressed whether it would be appropriate to increase the current \$250,000 threshold for transactions secured by residential real estate. The agencies determined that it would not be appropriate to increase the threshold for this category of transactions at this time based on three considerations. First, the agencies observed that any increase in the threshold for residential transactions would have a limited impact on burden, as appraisals would still be required for the vast majority of these transactions pursuant to rules of other federal government agencies and the government-sponsored enterprises (GSEs).<sup>25</sup> As reflected in the 2015 Home Mortgage Disclosure Act (HMDA) data,<sup>26</sup> at least 90 percent of residential mortgage loan originations had loan amounts at or below the threshold, were eligible for sale to GSEs, or were insured by the Federal Housing Administration or the United States Department of Veterans Affairs. Those transactions are not subject to the Title XI appraisal regulations, but the majority of those transactions are subject to the appraisal requirements of

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<sup>24</sup> The \$250,000 threshold in the current Title XI appraisal regulations applies, by its terms, to all real estate-related financial transactions, whether or not the borrower is a consumer.

<sup>25</sup> Other federal government agencies involved in the residential mortgage market include the U.S. Department of Housing and Urban Development (HUD), the U.S. Department of Veterans Affairs, and the Rural Housing Service of the U.S. Department of Agriculture. These agencies, along with the GSEs (which are regulated by the Federal Housing Finance Agency (FHFA)), have the authority to set separate appraisal requirements for loans they originate, acquire, or guarantee, and generally require an appraisal by a certified or licensed appraiser for residential mortgages regardless of the loan amount.

<sup>26</sup> See FFIEC, *Home Mortgage Disclosure Act*, [www.ffiec.gov/hmda/](http://www.ffiec.gov/hmda/).

other government agencies or the GSEs. Therefore, raising the appraisal threshold for residential transactions in the Title XI appraisal regulations would have limited impact on burden.

Second, appraisals can provide protection to consumers by helping to assure the residential purchaser that the value of the property supports the purchase price and the mortgage amount.<sup>27</sup> The consumer protection role of appraisals is reflected in amendments made to Title XI and the Truth in Lending Act (TILA)<sup>28</sup> through the Dodd-Frank Act governing the scope of transactions requiring the services of a certified or licensed appraiser. These include the addition of the CFPB to the group of agencies assigned a role in the appraisal threshold-setting process for Title XI,<sup>29</sup> and a new TILA provision requiring appraisals for loans involving “higher-risk mortgages.”<sup>30</sup>

During the EGRPRA process, the staff of the agencies conferred with the CFPB regarding comments the agencies received supporting an increase in the threshold for 1-to-4 family residential transactions. CFPB staff shared the view that appraisals can provide consumer protection benefits and their concern about potential risks to consumers resulting from an

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<sup>27</sup> The agencies posited in the 1994 amendments to the Title XI appraisal regulations that the timing of the appraisal may provide limited consumer protection. Changes to consumer protection regulations since 1994 now ensure that a consumer receives a copy of appraisals and other valuations used by a creditor to make a credit decision at least three business days before consummation of the transaction (for closed-end credit) or account opening (for open-end credit). See 12 CFR 1002.14 (for business or consumer credit secured by a first lien on a dwelling).

<sup>28</sup> 15 U.S.C. 1601 et seq.

<sup>29</sup> Dodd-Frank Act, Pub. L. 111-203, Title XIV, § 1473(a), 124 Stat. 2190 (2010), (codified at 12 U.S.C. 3341(b)), as discussed earlier in this **Supplementary Information**.

<sup>30</sup> “Higher risk mortgages” are certain mortgages with an annual percentage rate that exceeds the average prime offer rate by a specified percentage. See Dodd-Frank Act, Pub. L. 111-203, Title XIV, § 1471, 124 Stat. 2185 (2010), which added section 129H to TILA, (codified at 15 U.S.C. 1639h). See also Appraisals for Higher-Priced Mortgage Loans, 78 FR 78520 (December 26, 2013) (interagency rule implementing appraisal requirements for higher-priced mortgage loans).

expansion of the number of residential mortgage transactions that would be exempt from the Title XI appraisal requirement.

Third, the agencies considered safety and soundness concerns that could result from a threshold increase for residential transactions. As the EGRPRA Report noted, the 2008 financial crisis showed that, like other asset classes, imprudent residential mortgage lending can pose significant risks to financial institutions.

For these reasons, the agencies concluded in the EGRPRA Report that a change to the current \$250,000 threshold for residential mortgage loans would not be appropriate at the present time. The agencies are interested in comment on whether there are other factors that should be considered in evaluating the current threshold for 1-to-4 family residential transactions and whether the threshold can and should be raised, consistent with consumer protection, safety and soundness, and reduction of unnecessary regulatory burden. The agencies will also continue to consider possibilities for relieving burden related to appraisals for residential mortgage loans, such as coordination of the agencies' Title XI appraisal regulations with the practices of HUD, the GSEs, and other federal participants in the residential real estate market.

## **II. REVISIONS TO THE TITLE XI APPRAISAL REGULATIONS**

### ***A. Threshold Increase for Commercial Real Estate Transactions***

#### *Overview of Proposal*

The agencies propose to amend the Title XI appraisal regulations to increase the monetary threshold for commercial real estate transactions at or below which a Title XI appraisal

would not be required.<sup>31</sup> The proposal would establish a separate threshold for commercial real estate transactions of \$400,000, which represents an increase from the current threshold of \$250,000 for all real estate-related financial transactions.

In considering whether to propose an increased threshold for commercial real estate transactions, the agencies considered the comments received through the EGRPRA process, and took into account whether changes to the threshold would be appropriate to reduce regulatory burden consistent with the federal financial and public policy interests in real estate-related financial transactions and the safety and soundness of regulated institutions.

As stated, the threshold for exempt transactions was last modified in 1994. Given increases in commercial property values since that time, the current threshold requires institutions to obtain Title XI appraisals on a larger proportion of commercial real estate transactions than in 1994. This increase in the number of appraisals required may contribute to the increased burden in time and cost described by the EGRPRA commenters.

Based on supervisory experience and available data, the agencies propose to increase the threshold for commercial real estate transactions, as defined below, to \$400,000. This proposal would reduce burden for both rural and non-rural institutions and, as discussed below, would not pose a threat to the safety and soundness of financial institutions. The agencies are consulting with the CFPB regarding this proposal and will continue this consultation in developing a final rule.

The agencies propose to make the proposal, if adopted, effective on publication of the final rule in the Federal Register.<sup>32</sup>

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<sup>31</sup> The agencies have coordinated with the NCUA in developing this proposal. The agencies understand that the NCUA is evaluating options to develop a separate proposal to provide comparable relief for federally insured credit unions.

Question 1. The agencies invite comment on the proposed effective date, including whether this time period is appropriate and, if not, why.

*Definition of Commercial Real Estate Transaction*

The proposed \$400,000 threshold would apply only to transactions defined as “commercial real estate transactions.” Under the proposed definition, a commercial real estate transaction would include any “real estate-related financial transaction,” as defined in the Title XI appraisal regulations, excluding any loans secured by a 1-to-4 family residential property,<sup>33</sup> but including loans that finance the construction of buildings with 1-to-4 dwelling units and that do not include permanent financing.<sup>34</sup> Accordingly, the definition would include a loan extended

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<sup>32</sup> The Riegle Community Development and Regulatory Improvement Act of 1994, Pub. L. 103-325, 108 Stat. 2163 (Riegle Act) provides that rules imposing additional reporting, disclosures, or other new requirements on IDIs generally must take effect on the first day of a calendar quarter that begins on or after the date on which the regulations are published in final form. 12 U.S.C. 4802(b). As discussed further in the Section IV of the **Supplementary Information**, the proposed rule does not impose any new requirements on IDIs, and, as such, the effective date requirement of the Riegle Act is inapplicable. Additionally, the 30-day delayed effective date required under the Administrative Procedure Act (APA) is waived pursuant to 5 U.S.C. 553(d)(1), which provides a waiver when a substantive rule grants or recognizes an exception or relieves a restriction. The proposed rule would exempt certain transactions from the Title XI appraisal requirements. Consequently, the proposed rule meets the requirements for waiver set forth in the APA.

<sup>33</sup> A 1-to-4 family residential property is a property containing one, two, three, or four individual dwelling units, including manufactured homes permanently affixed to the underlying land (when deemed to be real property under state law). See OCC: 12 CFR Part 34 Subpart D, Appendix A; Board: 12 CFR 208, Appendix C; FDIC: 12 CFR Part 365, Subpart A, Appendix A.

<sup>34</sup> The second part of the definition is intended to clarify, not be an exception to, the first part.

to a consumer to finance the initial construction<sup>35</sup> of the consumer's dwelling, but exclude loans that provide both initial construction funding and permanent financing.<sup>36</sup>

The proposed definition would largely capture the following four categories of loans secured by real estate in the Consolidated Reports of Condition and Income (Call Report)<sup>37</sup> (FFIEC 031; RCFD 1410), namely loans that are: (1) for construction, land development, and other land loans; (2) secured by farmland; (3) secured by residential properties with five or more units; or (4) secured by nonfarm nonresidential properties. However, loans that provide both initial construction funding and permanent financing and are reported as construction, land development, and other land loans during the construction phase would be excluded from the definition.

The definition generally aligns with the categories of transactions to which agency guidance on commercial real estate lending applies.<sup>38</sup> The agencies are treating construction-

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<sup>35</sup> "Initial construction" refers to construction of a new dwelling, as opposed to improvements on an existing dwelling. This is intended to be consistent with the meaning of this phrase in provisions of the Truth in Lending Act and its implementing regulation, Regulation Z. *See, e.g.*, 15 U.S.C. § 1602(x); 12 CFR 1026.2(a)(24).

<sup>36</sup> The agencies propose to exclude consumer "construction-to-permanent" loans because these loans are, in effect, for the purchase of 1-to-4 family residential property, which would otherwise be subject to the \$250,000 threshold. This carve-out for construction-to-permanent financing would avoid the anomaly of requiring appraisals for permanent financing of 1-to-4 family residential properties above \$250,000 while allowing an evaluation for permanent financing (at or below \$400,000) that is preceded by a construction phase.

<sup>37</sup> *See* [https://www.ffiec.gov/pdf/FFIEC\\_forms/FFIEC031\\_201703\\_f.pdf](https://www.ffiec.gov/pdf/FFIEC_forms/FFIEC031_201703_f.pdf).

<sup>38</sup> Real Estate Lending: Interagency Statement on Prudent Risk Management for Commercial Real Estate Lending, OCC Bulletin 2015-51 (December 18, 2015); Statement on Prudent Risk Management for Commercial Real Estate Lending, Board SR Letter 15-17 (December 18, 2015); Statement on Prudent Risk Management for CRE Lending, FDIC FIL-62-2015 (December 18, 2015); Guidance on Prudent Loan Workouts, OCC Bulletin 2009-32 (October 30, 2009); Policy Statement on Prudent Commercial Real Estate Loan Workouts, Board SR Letter 09-07 (October 30, 2009); Policy Statement on Prudent Commercial Real Estate Loan Workouts, FDIC FIL-61-2009 (October 30, 2009); Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices, 71 FR 74580 (December 12, 2006).

only loans to consumers as commercial real estate transactions to maintain consistency with other regulations and guidance that address construction loans to consumers in other contexts.

Supervisory experience indicates that financial institutions generally administer construction loans to consumers in a way similar to construction loans to businesses. Therefore, subjecting most construction loans to the same threshold would minimize regulatory burden. This treatment would also be consistent with other mortgage-related rules, which exempt consumer construction loans from various consumer protection requirements.<sup>39</sup> The agencies believe that promoting consistency in definitions and structure across different regulations can reduce confusion and regulatory burden for financial institutions.

Moreover, including all 1-to-4 family residential construction-only loans in the proposed definition of commercial real estate transactions is consistent with the agencies' longstanding practice under the Title XI appraisal regulations of treating construction loans for 1-to-4 family residential properties as "nonresidential" for purposes of the requirement that certified appraisers be used for "nonresidential" federally related transactions.<sup>40</sup>

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<sup>39</sup> 78 FR 10368 (February 13, 2013) (exempting transactions to finance the initial construction of a dwelling from the higher-priced mortgage appraisal rule); 78 FR 4725 (January 22, 2013) (exempting transactions to finance the initial construction of a dwelling from the higher-priced mortgage escrow requirements); 78 FR 6408 (January 30, 2013) (exempting transactions to finance the initial construction of a dwelling from the ability-to-repay requirements); 78 FR 6856 (January 31, 2013) (exempting transactions to finance the initial construction of a dwelling from the high-cost mortgage loan term restrictions and disclosure requirements in the Home Ownership and Equity Protections Act); 76 FR 79772 (December 22, 2011) (exempting loans with maturity of 12 months or less for the construction primary dwelling from the balloon payment limitations).

<sup>40</sup> See OCC: 12 CFR 34.43(d); Board: 12 CFR 225.63(d)(2); FDIC: 12 CFR 323.3(d)(2). The agencies have long subjected such loans to this requirement, as opposed to permitting licensed appraisers, which is the case for typical 1-to-4 family residential properties.

As discussed further below, financial institutions report information about consumer construction loans aggregated with other construction loans through the Call Report.<sup>41</sup> Thus, much of the supervisory information that the agencies receive, including the basis for the analysis presented below, aggregates consumer construction loans with other construction loans secured by 1-to-4 residential properties.

Question 2. The agencies invite comment on the proposed definition of commercial real estate transaction.

Question 3. The proposed definition of commercial real estate transaction would include loans to consumers for the initial construction of their dwelling or transactions financing the construction of any building with 1-to-4 dwelling units, so long as the loan does not include permanent financing, with the effect of permitting these loans to qualify for the higher \$400,000 threshold. The agencies invite comment on the consumer, regulatory burden, and other implications of the proposal. What would be the implications of not including these loans in the definition, which would leave the current \$250,000 threshold in place?

Question 4. The agencies invite comment on the consumer, regulatory burden, and other implications of the proposed exclusion of construction-to-permanent loans from the definition of commercial real estate transaction, meaning that the current \$250,000 threshold would apply. What would be the implications of including construction-to-permanent loans in the definition of commercial real estate transaction, thus allowing these loans to qualify for the higher \$400,000 threshold?

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<sup>41</sup> See series RCFD F158 and F159.

### *Threshold Increase*

The agencies propose to increase the threshold in the Title XI appraisal regulations for commercial real estate transactions from \$250,000 to \$400,000. In determining the level of increase, the agencies considered the change in prices for commercial real estate measured by the Federal Reserve Commercial Real Estate Price Index (“CRE Index”). The CRE Index<sup>42</sup> is a direct measure of the changes in commercial real estate prices in the United States.<sup>43</sup> The CRE Index is comprised of data from the CoStar Commercial Repeat Sale Index,<sup>44</sup> which uses repeat sale regression analysis of 1.7 million commercial property sales records to compare the change in price for the same property between its most recent and previous sale transactions.<sup>45</sup> The data incorporated into this index covers properties across the country and across all price ranges,<sup>46</sup> from before 1994 through the present.

Based on a review of the CRE Index, prices for commercial real estate have increased since 1994, resulting in an increased proportion of commercial real estate transactions exceeding

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<sup>42</sup> The Board publishes data on the flow of funds and levels of financial assets and liabilities, by sector and financial instrument; full balance sheets, including net worth, for households and nonprofit organizations, nonfinancial corporate businesses, and nonfinancial noncorporate businesses; Integrated Macroeconomic Accounts; and additional supplemental detail. See, Board of Governors of the Federal Reserve System, Financial Accounts of the United States, <https://www.federalreserve.gov/releases/z1/current/default.htm>.

<sup>43</sup> The CRE Index is quarterly and not seasonally adjusted. See Board of Governors of the Federal Reserve System, Series analyzer for FL075035503.Q, <https://www.federalreserve.gov/apps/fof/SeriesAnalyzer.aspx?s=FL075035503&t=&bc=:FI075035503,FL075035503&suf=Q>; Board of Governors of the Federal Reserve System, Series Structure, <https://www.federalreserve.gov/apps/fof/SeriesStructure.aspx>.

<sup>44</sup> Board of Governors of the Federal Reserve System, Series analyzer for FL075035503.Q, <https://www.federalreserve.gov/apps/fof/SeriesAnalyzer.aspx?s=FL075035503&t=&bc=:FI075035503,FL075035503&suf=Q>. Data for years prior to 1996 are comprised of a weighted average of three appraisal-based commercial property series from National Real Estate Investor. Id.

<sup>45</sup> CoStar, *Federal Reserve’s Flow of Funds to Incorporate CoStar Group’s Price Indices*, CoStar (June 4, 2012), <http://www.costar.com/News/Article/Federal-Reserves-Flow-of-Funds-To-Incorporate-CoStar-Groups-Price-Indices/138998>.

<sup>46</sup> See id.

the threshold level today compared to 1994. Based on the change in the CRE Index, a commercial property that sold for \$250,000 as of June 30, 1994 would be expected to sell for approximately \$830,000 as of December 2016. However, as shown below in Table 1, the price of commercial real estate can be particularly volatile. For example, the CRE Index indicates a commercial property that sold for \$250,000 in 1994 would be expected to sell for approximately \$412,000 in December 2003, \$711,000 in December 2007, and \$423,000 in March 2010, when commercial real estate prices were at their lowest point in the most recent downturn.

In proposing to raise the commercial real estate threshold to \$400,000 the agencies are approximating prices at the low point of the most recent cycle, which occurred in 2010. This more conservative approach is appropriate because it takes into consideration the volatility in actual prices of commercial real estate over time.

This figure is also consistent with general measures of inflation across the economy since 1994, when the current threshold of \$250,000 was set. The agencies considered general inflation indices, including the Consumer Price Index (CPI)<sup>47</sup> and the Personal Consumption Expenditures Price Index (PCE).<sup>48</sup> Certain price changes tracked by these general indices indirectly affect commercial real estate values. For example, the change in rents for multifamily housing affects the value of underlying properties, and the change in prices of consumer products affects the

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<sup>47</sup> The CPI, which is published by the Bureau of Labor Statistics (BLS), is a measure of the average change over time in the prices paid by urban consumers for a market basket of goods and services. This series is published monthly and is not seasonally adjusted. See U.S. Dept. of Labor Statistics, *Consumer Price Index*, <https://www.bls.gov/cpi/>.

<sup>48</sup> The PCE, which is published by the Bureau of Economic Analysis within the U.S. Department of Commerce, is the broadest measure of the average change over time of the price of consumer goods and services. This series is published monthly and is seasonally adjusted. See U.S. Department of Commerce, Bureau of Economic Analysis, *Consumer Spending*, [https://www.bea.gov/national/consumer\\_spending.htm](https://www.bea.gov/national/consumer_spending.htm); Federal Reserve Bank of San Francisco, *PCE Inflation Dispersion*, <http://www.frbsf.org/economic-research/indicators-data/pce-personal-consumption-expenditure-price-index-pcepi/>.

value of retail and warehouse space. While these indices are not directly based on changes in commercial real estate prices, general inflation is a component of the change in commercial real estate values.

As indicated in the table below, when adjusting a \$250,000 basket of goods under the CPI and PCE from 1994 dollars to 2017 dollars and using a lowest point in the cycle adjustment for the prices for commercial real estate under the CRE Index, each of the indices considered approximately tracks the \$400,000 proposed threshold.

Table 1: Inflation Adjustments of \$250,000 at June 30, 1994, for the CRE Index; July 1994 for the CPI Index and July 1, 1994, for the PCE Index.

<b>Index source:</b>	<b>Index series:</b>	<b>Dated Adjusted To</b>	<b>Adjusted Amount</b>
CRE Index	Flow of Funds	December 2016	\$830,674
		March 2010	\$423,659
		December 2007	\$711,367
		December 2003	\$412,194
CPI	All items, US	March 2017	\$401,166
PCE	All products	March 2017	\$373,706

Question 5. The agencies invite comment on the proposed level of \$400,000 for the threshold at or below which regulated institutions would not be required to obtain appraisals for commercial real estate transactions.

Question 6. How would having three threshold levels (\$250,000 for all transactions, \$400,000 for commercial real estate transactions, and \$1 million for qualifying business loans) rather than two threshold levels applicable to Title XI appraisals within the appraisal regulations affect burden to applicable institutions?

*Safety and Soundness Considerations for Increasing the Threshold for Commercial Real Estate Transactions*

Under Title XI, the agencies may set a threshold at or below which an appraisal performed by a state certified or licensed appraiser is not required if they determine in writing that such a threshold level does not pose a threat to the safety and soundness of financial institutions.<sup>49</sup> Analysis of supervisory experience and available data indicates that the proposed threshold level of \$400,000 for commercial real estate transactions would not pose a threat to the safety and soundness of financial institutions.

Many variables, including changing market conditions and various loan underwriting practices, may affect an institution's loss experience. The \$250,000 threshold has been applicable to commercial real estate transactions since 1994. Analysis of supervisory information concerning losses on commercial real estate transactions suggests that faulty valuations of the underlying real estate collateral have not been a material cause of losses in connection with transactions at or below \$250,000. In the last three decades, the banking industry suffered two crises in which poorly underwritten and administered commercial real estate loans were a key feature in elevated levels of loan losses and bank failures.<sup>50</sup> Supervisory experience and a review of material loss reviews<sup>51</sup> covering those decades suggests that larger

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<sup>49</sup> 12 U.S.C. 3341(b).

<sup>50</sup> See, e.g., Federal Deposit Insurance Corporation, *History of the Eighties – Lessons for the Future, Chapter 3: Commercial Real Estate and the Banking Crises of the 1980s and Early 1990s*, available at [https://www.fdic.gov/bank/historical/history/137\\_165.pdf](https://www.fdic.gov/bank/historical/history/137_165.pdf); Federal Deposit Insurance Corporation, Office of the Inspector General, EVAL-13-002, *Comprehensive Study on the Impact of the Failure of Insured Depository Institutions* 50, Table 6 (January 2013), available at <https://www.fdicig.gov/reports13/13-002EV.pdf>.

<sup>51</sup> Section 38(k) of the FDI Act, as amended, provides that if the Deposit Insurance Fund incurs a “material loss” with respect to an IDI, the Inspector General of the appropriate regulator (which for the OCC is the Inspector General of the Department of the Treasury) shall prepare a report to

acquisition, construction, and development<sup>52</sup> transactions were more likely to be troublesome due to the lack of appropriate underwriting and administration of issues unique to larger properties, such as longer construction periods, extended “lease up” periods (the time required to lease a building after construction), and the more complex nature of the construction of such properties. The agencies have no evidence that increasing the appraisal threshold to \$400,000 for commercial real estate transactions would materially increase the risk of loss on such transactions.

### **Coverage of the Threshold**

The agencies’ analysis of available data<sup>53</sup> related to commercial real estate lending at financial institutions suggests that an increase in the threshold would not pose a safety and soundness risk to financial institutions.

In order to consider the potential impact of the proposed threshold change on safety and soundness, the agencies considered how the coverage of transactions exempted by the threshold would change, both in terms of number of transactions and aggregate value. The agencies considered three different metrics to estimate the overall coverage of the existing threshold and the proposed threshold: the number of commercial real estate transactions at or under the threshold as a share of the number of all commercial real estate transactions; the dollar volume of commercial real estate transactions at or under the threshold as a share of the total dollar volume of all commercial real estate transactions; and the dollar volume of commercial real estate

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that agency, identifying the cause of failure and reviewing the agency’s supervision of the institution. 12 U.S.C. 1831o(k).

<sup>52</sup> Acquisition, development and construction refers to transactions that finance construction projects including land, site development, and vertical construction. This type of financing is typically recorded in the land or construction categories of the Call Report.

<sup>53</sup> The agencies have examined data from a number of different sources to evaluate the impact of the proposed change in the appraisal threshold on the safety and soundness of financial institutions, as no single data source is sufficient alone to fully analyze the impact.

transactions at or under the threshold relative to IDIs' capital and the allowance for loan and lease losses, which act as a buffer to absorb losses, as explained below. The agencies examined data reported on the Call Report<sup>54</sup> and data from the CoStar Comps database to estimate the volume of commercial real estate transactions covered by the existing threshold and increased thresholds.

### *Analysis of Call Report Data*

The agencies' analysis of data reported on the Call Report suggests that the threshold for commercial real estate transactions could be raised without exceeding the risk that these transactions posed when the thresholds were established in 1994.

All FDIC-insured depository institutions report information about loans on their balance sheets by category of loan,<sup>55</sup> but because IDIs do not report on loans in all of the categories that would be included in the definition of commercial real estate transaction by loan size, the

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<sup>54</sup> The agencies used data reported on Schedule RC-C and RC-C Part II of the Call Report. Schedule RC-C includes the dollar volume of all loans secured by real estate, reported in the five categories: (1) for construction, land development, and other land loans (RCFD F158 and F159); (2) secured by farmland (RCFD 1420); (3) secured by residential properties with five or more units (RCFD 1460); or (4) secured by nonfarm nonresidential properties (RCFD F160 and F161); and (5) secured by residential properties with fewer than five dwelling units (RCFD 1797, 5367, and 5368). As discussed earlier in this **Supplementary Information**, the fifth category would not be included in the definition of commercial real estate transaction. Schedule RC-C Part II, Loans to Small Businesses and Farms, includes the number and amount currently outstanding in each case reported in groupings by loan amount of loans secured by nonfarm, nonresidential real estate, with original amounts of \$1,000,000 or less and loans secured by farmland with original amounts of \$500,000 or less. Institutions do not report information on the size of land and construction or multifamily loans. See Federal Financial Institutions Examination Council, *Consolidated Reports of Condition and Income for a Bank with Domestic and Foreign Offices – FFIEC 031*, [https://www.ffiec.gov/pdf/FFIEC\\_forms/FFIEC031\\_201703\\_f.pdf](https://www.ffiec.gov/pdf/FFIEC_forms/FFIEC031_201703_f.pdf).

<sup>55</sup> See Federal Deposit Insurance Corporation, Bank Financial Reports, Consolidated Reports of Condition and Income, <https://www.fdic.gov/regulations/resources/call/index.html>. (“Every national bank, state member bank, insured state nonmember bank, and savings association (‘institution’) is required to file Call Report as of the close of business on the last day of each calendar quarter, i.e., the report date. The specific reporting requirements depend upon the size of the institution, the nature of its activities, and whether it has any foreign offices.”).

agencies used loans secured by nonfarm, nonresidential real estate (NFNR loans) as a proxy for commercial real estate transactions in this analysis.<sup>56</sup> Data on NFNR loans are an effective proxy because the vast majority of commercial real estate transactions are in the NFNR category. NFNR loans should mirror trends across all categories of commercial real estate transactions.

IDIs report information on NFNR loans in the Call Report by three separate size categories: 1) loans with original amounts of \$100,000 or less; 2) loans with original amounts of more than \$100,000, but \$250,000 or less; and 3) loans with original amounts of more than \$250,000, but \$1,000,000 or less. They separately report the dollar amount of all NFNR loans, including those over \$1,000,000. Using this data, the agencies calculated the dollar amount of NFNR loans at or under the current \$250,000 threshold as a percentage of the dollar amount of all NFNR loans.

According to Call Report data, when the threshold for real-estate related financial transactions was raised from \$100,000 to \$250,000 in 1994, approximately 18 percent of the dollar volume of all NFNR loans reported by IDIs had original loan amounts of \$250,000 or less. As of the fourth quarter of 2016, approximately 4 percent of the dollar volume of such loans had original loan amounts of \$250,000 or less. This analysis suggests that a larger proportion of commercial real estate transactions now require appraisals than when the threshold was last established.

In contemplating an increase in the threshold for commercial real estate transactions, the agencies also used Call Report data to consider the transactions exempted from the appraisal

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<sup>56</sup> Although farmland is reported by size of loan, such loans were also excluded from the analysis, because they comprise a very small percent of overall commercial real estate transactions and are unlikely to materially affect the analysis. Moreover, the majority of farmland loans are considered qualifying business loans and are eligible for the higher \$1,000,000 threshold.

threshold as a share of equity capital plus the allowance for loan and lease losses (the allowance), which is a measure of the potential concentration risk that these transactions could pose to the financial well-being of institutions as a whole. In 1994, NFNR loans with original loan amounts of \$250,000 or less represented in the aggregate approximately 14 percent of IDIs' equity capital plus the allowance. By the fourth quarter of 2016, such loans represented only about 3 percent of IDIs' equity capital plus the allowance.

To determine whether concentration risk would be similar for small institutions, the agencies separately considered the percentage of NFNR transactions exempted from the appraisal threshold as a share of equity capital plus the allowance for IDIs with assets of less than \$1 billion. This analysis produced similar results. Approximately 30 percent of the dollar volume of all NFNR loans in such smaller institutions had original loan amounts of \$250,000 or less in 1994. By the fourth quarter of 2016, however, only about 11 percent of the dollar volume of such loans had original loan amounts of \$250,000 or less. In 1994, the dollar volume of smaller IDIs' NFNR loans with original loan amounts of \$250,000 or less represented approximately 33 percent of equity capital plus the allowance. These loans represented only about 18 percent of IDIs' equity capital plus the allowance by the fourth quarter of 2016.

Because IDIs report loans on the Call Report aggregated into only the three categories mentioned above (less than \$100,000, \$100,000 to \$250,000, and \$250,000 to \$1,000,000), the agencies cannot use Call Report data to determine the precise percentage or number of transactions that would be exempted by the proposed \$400,000 threshold or the precise impact of a \$400,000 threshold on equity capital plus the allowance.

*Analysis of CoStar Comps Data*

As described below, the agencies have used the CoStar Comps database to estimate this impact. The CoStar Comps database<sup>57</sup> provides sales value data on specific commercial real estate transactions. While there are some limitations regarding use of the CoStar Comps database, as detailed below, the database contains information on sales values for individual transactions, so it can be used to estimate the number and percentage of transactions that would become exempt under the proposed threshold change (*i.e.*, those above \$250,000, but less than \$400,000).<sup>58</sup>

The CoStar Comps database contains data for transactions involving nonresidential commercial mortgages, multifamily and land. The CoStar Comps database is derived from sales data and reflects the total transaction amount, as opposed to the loan amount. For purposes of this analysis, the agencies included only financed transactions and assumed a loan-to-value ratio of 85 percent for non-residential and multi-family commercial mortgages and a loan-to-value ratio of 65 percent for raw land transactions<sup>59</sup> to arrive at an estimated loan amount which would be equivalent to the “transaction value” under the Title XI appraisal regulations. While the CoStar Comps database has some limitations for the purposes of evaluating the proposed

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<sup>57</sup> The CoStar Comps database is comprised of sales data involving commercial real estate properties. The agencies have limited their analysis to arms-length completed sales, where the price is provided. The agencies have also limited the sample to properties that were financed. Owner-occupied properties and sales of coops and condominiums were excluded. The sample was also limited to existing buildings. Land includes only raw land defined as land held for development or held for investment.

<sup>58</sup> This same analysis could not be performed using Call Report data because, as described above, transactions reported for purposes of the Call Report are either reported in groupings of large value ranges or not reported by size at all.

<sup>59</sup> The Interagency Guidelines for Real Estate Lending provides that institutions’ loan-to-value limits should not exceed 85 percent for loans secured by improved property and 65 percent for loans secured by raw land. See OCC: 12 CFR Part 34, Subpart D, Appendix A; Board: 12 CFR Part 208, Appendix C; FDIC: 12 CFR Part 365, Subpart A, Appendix A.

increase,<sup>60</sup> it provides information that can be used to estimate the dollar volume and number of commercial real estate transactions that would potentially be exempted by the proposed threshold increase.

An analysis of the CoStar Comps database suggests that increasing the threshold to \$400,000 would significantly increase the number of commercial real estate transactions exempted from the Title XI appraisal requirements, but the portion of the total dollar size of commercial real estate transactions that would remain exempted by the threshold would be minimal. The percentage of commercial properties with loans in the CoStar Comps database that would be exempted from the Title XI appraisal regulations by the threshold would increase from 17 percent to 28 percent if the threshold were raised from \$250,000 to \$400,000. However, the total dollar volume of loans for commercial properties in the CoStar Comps database would only increase from 0.7 percent to 1.5 percent.

Exempting an additional 11 percent of commercial real estate transactions would provide burden relief as sought by some of the EGRPRA commenters. The 0.8 percentage point increase in the dollar volume of commercial real estate transactions that the CoStar data suggests would be exempted from the appraisal requirements under the proposed threshold is unlikely to expose financial institutions to increased safety and soundness risk.

### **Analysis of Charge-Off Rates**

In addition to assessing changes in the magnitude of transactions covered by the appraisal threshold, the agencies assessed trends in the loss rate experience of commercial real estate transactions.

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<sup>60</sup> For example, the database tends to underrepresent sales of smaller properties and transactions in rural markets, and includes transactions that are not financed by depository institutions.

While the agencies do not regularly collect data on rates of loss for commercial real estate by the size of loans, they do collect net charge-off<sup>61</sup> data for commercial real estate loans on the Call Report. The agencies considered aggregate net charge-off rates for commercial real estate loans in determining whether the threshold would pose a threat to the safety and soundness of financial institutions.<sup>62</sup>

In order to evaluate the impact of commercial real estate lending on the safety and soundness of the banking system generally, the agencies compared peak net charge-off rates for two periods: 1991 to 1994 and 2007 to 2012. These periods represent two distress cycles when aggregate net charge offs rose to their highest levels. The agencies separately examined charge-off rates on lending for all commercial real estate categories covering construction, multifamily, non-farm, non-residential, and farmland. In order to evaluate whether commercial real estate lending may have a disparate impact on the safety and soundness of IDIs of varying sizes, the agencies examined peak charge-off rates on loans for all IDIs, IDIs under one billion dollars in total assets, IDIs with total assets between one billion dollars and ten billion dollars, and IDIs with total assets of more than ten billion dollars.

The analysis showed that aggregate peak net charge-off rates for the most recent cycle were generally no worse than those recorded for the prior cycle, with the exception of construction loans. Moreover, aggregate commercial real estate loan loss rates for banks less than \$1 billion (which would reasonably be expected to have a larger proportion of small loans, given their lower legal lending limits due to their smaller size) were lower than for larger banks as a group.

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<sup>61</sup> Net charge-offs are charge-offs minus recoveries.

<sup>62</sup> Net charge-offs represent losses to financial institutions, which, in the aggregate, can pose a threat to safety and soundness.

This data suggests that the loss experience associated with commercial real estate loans for the banking system as a whole has stayed at a relatively consistent rate through multiple credit cycles. Thus, banking system safety and soundness concerns associated with the commercial real estate loan loss rates have not increased. However, commercial real estate loan charge-off rates during periods of economic stress have and will continue to vary across individual IDIs based on location, collateral, quality of underwriting and risk management, and other factors. Thus commercial real estate loan concentration risk at individual institutions remains a focus for the banking agencies.

Question 7. The agencies invite comment on the safety and soundness impact of the proposed \$400,000 threshold for commercial real estate transactions.

Question 8. The agencies invite comment on the data used in this analysis, and what alternative sources of data would be appropriate for this analysis.

### ***B. Use of Evaluations***

The Title XI appraisal regulations require regulated institutions to obtain evaluations for three categories of real estate-related financial transactions that the agencies have determined do not require a Title XI appraisal, including real-estate related financial transactions at or below the \$250,000 threshold and qualifying business loans at or below the \$1,000,000 threshold. Similarly, the agencies propose to require that institutions entering into commercial real estate transactions at or below the proposed \$400,000 threshold obtain evaluations that are consistent with safe and sound banking practices for such transactions.<sup>63</sup>

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<sup>63</sup> When a below-threshold transaction also qualifies for an exemption from the appraisal requirements for a reason other than being below one of the thresholds or a qualifying existing extension of credit, no evaluation is required.

An evaluation provides a general estimate of the value of real estate, but is not subject to the same requirements as a Title XI appraisal. An evaluation should provide appropriate information to enable the institution to make a prudent decision regarding the transaction. Through the Guidelines, the agencies have provided guidance to regulated institutions on their expectations regarding when and how evaluations should be used. The Guidelines describe the transactions for which financial institutions are required to obtain an evaluation, and recommend that institutions develop policies and procedures for identifying when to obtain appraisals for such transactions.

Institutions should conduct evaluations consistent with the provisions in the Guidelines.<sup>64</sup> As described in the Guidelines, evaluations should be performed by persons who are competent and have the relevant experience and knowledge of the market, location, and type of real property being valued.<sup>65</sup> Evaluations may be completed by a bank employee or by a third party, as explained by the Interagency Advisory on Use of Evaluations in Real Estate-Related Financial Transactions.<sup>66</sup> Guidance on achieving independence in the collateral valuation program can be found in the Guidelines, among other sources.<sup>67</sup> The Guidelines state that an evaluation should provide an estimate of the property's market value or sufficient information and analysis to support the credit decision. The Guidelines also describe the minimum content that an evaluation should contain.

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<sup>64</sup> Guidelines at 75 FR 77461.

<sup>65</sup> Interagency Appraisal and Evaluations Guidelines, 75 FR 77450, at 77458 (December 10, 2010).

<sup>66</sup> Interagency Advisory on Use of Evaluations in Real Estate-Related Financial Transactions, OCC Bulletin 2016-8 (March 4, 2016); Board SR Letter 16-05 (March 4, 2016); Supervisory Expectations for Evaluations, FDIC FIL-16-2016 (March 4, 2016).

<sup>67</sup> Guidelines at 75 FR 77457-58. See also Valuation Independence rules in Regulation Z, which apply to all creditors and cover extensions of consumer credit that are or will be secured by a consumer's principal dwelling: Board: 12 CFR 226.42; CFPB: 12 CFR 1026.42.

In evaluating this proposal, the agencies considered the impact to the financial system of the proposal, and specifically the impact to financial institutions and borrowers of obtaining evaluations instead of Title XI appraisals. Based on information from industry participants, the cost of third-party evaluations of commercial real estate generally ranges from \$500 to over \$1,500, whereas the cost of appraisals of such properties generally ranges from \$1,000 to over \$3,000. Commercial real estate transactions with transaction values above \$250,000 but at or below \$400,000 (affected transactions), are likely to involve smaller and less complex properties, and appraisals and evaluations on such properties would likely be at the lower end of the cost range. This third-party pricing information suggests a savings of several hundred dollars per affected transaction.

The agencies also considered the costs in terms of time to obtain and process appraisals and evaluations. There may be less delay in finding appropriate personnel to perform an evaluation than to perform a Title XI appraisal, particularly in rural areas. As described in the Guidelines, financial institutions should review the property valuation prior to entering into the transaction. Financial institutions require less time to review evaluations than to review appraisals, because evaluations contain less detailed information. The agencies estimate that, on average, the review process for an appraisal would take approximately forty minutes and the review process for an evaluation would take approximately ten minutes. Thus, for affected transactions, the proposed rule would alleviate approximately thirty minutes of employee time per transaction, in addition to the reduced delay and the cost savings of obtaining an evaluation instead of an appraisal.

In considering the aggregate effect of this proposal, the agencies considered the number of affected transactions. As previously discussed, the agencies estimate that the number of

commercial real estate transactions that would be exempted by the threshold is expected to increase by approximately 11 percent under the proposed rule. Thus, while the precise number of affected transactions and the precise cost reduction per transaction cannot be determined, the proposed rule is expected to lead to significant cost savings for institutions that engage in commercial real estate lending.

Question 9. The agencies invite comment on the proposed requirement that regulated institutions obtain evaluations for commercial real estate transactions at or below the \$400,000 threshold.

Question 10. What type of additional guidance, if any, do institutions need to support the increased use of evaluations?

Question 11. To what extent does the use of evaluations reduce burden and cost over the use of appraisals? To what extent are evaluations currently done by in-house staff versus outsourced to appraisers or other qualified professionals?

### ***C. State Certified Appraiser Required***

The current Title XI appraisal regulations, require that “[a]ll federally related transactions having a transaction value of \$250,000 or more, other than those involving appraisals of 1-to-4 family residential properties, shall require an appraisal prepared by a State certified appraiser.”<sup>68</sup> In order to make this paragraph consistent with the other proposed changes to the appraisal regulations, the agencies are proposing a change to its wording to introduce the \$400,000 threshold and use the term “commercial real estate transaction.” The amendment to this provision would be a technical change that would not alter any substantive requirement.

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<sup>68</sup> OCC: 12 CFR 34.43(d); Board: 12 CFR 225.63(d)(2); FDIC: 12 CFR 323.3(d)(2).

### ***III. APPRAISAL THRESHOLD FOR QUALIFYING BUSINESS LOANS***

As noted above, in the 2017 EGRPRA Report to Congress, the agencies stated their intention to gather more information about the appropriateness of increasing the \$1 million threshold for qualifying business loans. The agencies are not proposing an increase in the business loan threshold at this time, but the agencies invite comment on the following questions concerning the qualifying business loan exemption:

Question 12. The agencies invite comment and supporting data on the appropriateness of raising the current \$1,000,000 threshold for qualifying business loans and the associated implications for safety and soundness.

Question 13. What unique risks do institutions associate with qualifying business loans?

Question 14. What percentage of total real estate lending at financial institutions, by number of loans and dollar volume of lending, are qualifying business loans?

Question 15. What is the average size of a qualifying business loan at financial institutions? What are the incidences of default on qualifying business loans compared to other commercial real estate transactions that institutions have observed over time?

Question 16. The agencies invite comment on the clarity of the application of the current threshold for qualifying business loans, and on any difficulty that financial institutions have experienced in interpreting the limitation on source of repayment.

### ***IV. REQUEST FOR COMMENTS***

The Agencies invite comment on all aspects of the proposed rulemaking.

Question 17. As discussed earlier, the agencies have articulated several bases for declining to propose an increase in the residential threshold. The agencies request comment on

whether there are other factors that should be considered in evaluating the current appraisal threshold for 1-to-4 family residential properties.

## ***V. REGULATORY ANALYSIS***

### ***A. Regulatory Flexibility Act***

**OCC:** The Regulatory Flexibility Act (RFA), 5 U.S.C. 601 et seq., generally requires that, in connection with a rulemaking, an agency prepare and make available for public comment a regulatory flexibility analysis that describes the impact of the rule on small entities. However, the regulatory flexibility analysis otherwise required under the RFA is not required if an agency certifies that the rule will not have a significant economic impact on a substantial number of small entities (defined in regulations promulgated by the Small Business Administration (SBA) to include commercial banks and savings institutions, and trust companies, with assets of \$550 million or less and \$38.5 million or less, respectively) and publishes its certification and a brief explanatory statement in the **Federal Register** together with the rule.

The OCC currently supervises approximately 956 small entities. Data currently available to the OCC are not sufficient to estimate how many OCC-supervised small entities make CRE loans in amounts that fall between the current and proposed thresholds. Therefore, we cannot estimate how many small entities may be affected by the increase threshold. However, because the proposal does not contain any new recordkeeping, reporting, or compliance requirements, the proposal will not impose costs on any OCC-supervised institutions. Accordingly, the OCC certifies that the proposed rule will not have a significant economic impact on a substantial number of small entities.

**Board:** The RFA,<sup>69</sup> requires an agency either to provide an initial regulatory flexibility analysis with a proposed rule or certify that the proposed rule will not have a significant economic impact on a substantial number of small entities. The proposed threshold increase applies to certain IDIs and non-bank entities that make loans secured by commercial real estate.<sup>70</sup> The Small Business Administration (SBA) establishes size standards that define which entities are small businesses for purposes of the RFA.<sup>71</sup> The size standard to be considered a small business is: \$550 million or less in assets for banks and other depository institutions; and \$38.5 million or less in annual revenues for the majority of non-bank entities that are likely to be subject to the proposed regulation.<sup>72</sup> Based on the Board's analysis, and for the reasons stated below, the proposed rule may have a significant positive economic impact on a substantial number of small entities. Accordingly, the Board is publishing an initial regulatory flexibility analysis. The Board will conduct a final regulatory flexibility analysis after consideration of comments received during the public comment period.

The Board requests public comment on all aspects of this analysis.

#### **A. Reasons for the Proposed Rule**

In response to comments received in the EGRPRA process, the agencies are proposing to increase the threshold from \$250,000 to \$400,000 at or below which a Title XI appraisal is not require for commercial real estate transactions. Because commercial real estate prices have increased since 1994, when the current \$250,000 threshold was established, a smaller percentage

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<sup>69</sup> 5 U.S.C. 601 *et seq.*

<sup>70</sup> For its RFA analysis, the Board considered all Board-regulated creditors to which the proposed rule would apply.

<sup>71</sup> U.S. SBA, Table of Small Business Size Standards Matched to North American Industry Classification System Codes, available at [https://www.sba.gov/sites/default/files/files/Size\\_Standards\\_Table.pdf](https://www.sba.gov/sites/default/files/files/Size_Standards_Table.pdf).

<sup>72</sup> Asset size and annual revenues are calculated according to SBA regulations. See 13 CFR 121 *et seq.*

of commercial real estate transactions are currently exempted from the Title XI appraisal requirements than when the threshold was established. This threshold adjustment is intended to reduce the regulatory burden associated with extending credit secured by commercial real estate in a manner that is consistent with safety and soundness of financial institutions.

## **B. Statement of Objectives and Legal Basis**

As discussed above, the agencies' objective in proposing this threshold increase is to reduce the regulatory burden associated with extending credit in a safe and sound manner by reducing the number of commercial real estate transactions that are subject to the Title XI appraisal requirements.

Title XI explicitly authorizes the agencies to establish a threshold level at or below which a Title XI appraisal is not required if the agencies determine in writing that the threshold does not represent a threat to the safety and soundness of financial institutions and receive concurrence from the Bureau of Consumer Financial Protection that such threshold level provides reasonable protection for consumers who purchase 1-to-4 unit single-family homes.<sup>73</sup> Based on available data and supervisory experience, the agencies tailored the size and scope of the proposed threshold increase to ensure that it would not pose a threat to safety and soundness of financial institutions or erode protections for consumers who purchase 1-to-4 unit single-family homes.

The Board's proposed rule would apply to state chartered banks that are members of the Federal Reserve System (state member banks), as well as bank holding companies and nonbank subsidiaries of bank holding companies that engage in lending. There are approximately 601 state member banks and 35 nonbank lenders regulated by the Board that meet the SBA definition

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<sup>73</sup> 12 U.S.C. 3341(b).

of small entities and would be subject to the proposed rule. Data currently available to the Board do not allow for a precise estimate of the number of small entities that would be affected by the proposed rule because the number of small entities that will engage in commercial real estate transactions within the proposed threshold is unknown.

### **C. Projected Reporting, Recordkeeping and Other Compliance Requirements**

The proposed rule would reduce reporting, recordkeeping, and other compliance requirements for small entities. For transactions at or below the proposed threshold, regulated institutions would be given the option to obtain an evaluation of the property instead of an appraisal. Unlike appraisals, evaluations may be performed by a lender's own employees and are not required to comply with USPAP. As discussed in detail in Section II.B of the **Supplementary Information**, the cost of obtaining appraisals and evaluations can vary widely depending on the size and complexity of the property, the party performing the valuation, and market conditions where the property is located. Additionally, the costs of obtaining appraisals and evaluations may be passed on to borrowers. Because of this variation in cost and practice, it is not possible to precisely determine the cost savings that regulated institutions will experience due to the decreased cost of obtaining an evaluation rather than an appraisal. However, based on information available to the Board, it is likely that small entities and borrowers engaging in commercial real estate transactions could experience significant cost reductions.

In addition to costing less to obtain than appraisals, evaluations also require less time to review than appraisals because they contain less detailed information. As discussed further in Section II.B of the **Supplementary Information**, an appraisal takes approximately forty minutes to review and an evaluation takes approximately ten minutes to review. Thus, the proposed rule would alleviate approximately thirty minutes of employee time per affected transaction for which the lender obtains an evaluation instead of an appraisal.

As previously discussed, the Board estimates that the percentage of commercial real estate transactions that would be exempted by the threshold is expected to increase by approximately 11 percent under the proposed rule. The Board expects this percentage to be higher for small entities, because a higher percentage of their loan portfolios are likely to be made up of small, below-threshold loans than those of larger entities. Thus, while the precise number of transactions that will be affected and the precise cost reduction per transaction cannot be determined, the proposed rule is expected to have a significant positive economic impact on small entities that engage in commercial real estate lending.

#### **D. Identification of Duplicative, Overlapping, or Conflicting Federal Regulations**

The Board has not identified any Federal statutes or regulations that would duplicate, overlap, or conflict with the proposed revisions.

#### **E. Discussion of Significant Alternatives**

The agencies considered additional burden-reducing measures, such as increasing the commercial threshold to a higher dollar amount and increasing the residential and business loan thresholds, but have not proposed such measures at this time for the safety and soundness and consumer protection reasons previously discussed. For transactions exempted from the Title XI appraisal requirements, the proposed rule would require regulated institutions to get an evaluation if they do not get an appraisal. The agencies believe this requirement is necessary to protect the safety and soundness of financial institutions, which is a legal prerequisite to the establishment of any threshold. The Board is not aware of any other significant alternatives that would reduce burden on small entities without sacrificing the safety and soundness of financial institutions or consumer protections.

*FDIC:* The RFA generally requires that, in connection with a notice of proposed rulemaking, an agency prepare and make available for public comment an initial regulatory

flexibility analysis describing the impact of the proposed rule on small entities.<sup>74</sup> A regulatory flexibility analysis is not required, however, if the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. The SBA has defined “small entities” to include banking organizations with total assets less than or equal to \$550 million.<sup>75</sup> For the reasons described below and pursuant to section 605(b) of the RFA, the FDIC certifies that the final rule will not have a significant economic impact on a substantial number of small entities.

The FDIC supervises 3,744 depository institutions,<sup>76</sup> of which, 3,028 are defined as small banking entities by the terms of the RFA.<sup>77</sup> According to the Call Report 3,010 small entities reported holding some volume of real estate related financial transactions that meet the proposed rule’s definition of a commercial real estate transaction.<sup>78</sup> Therefore, 3,010 small entities could be affected by the proposed rule.

The proposed rule will raise the appraisal threshold for commercial real estate transactions from \$250,000 to \$400,000. Any commercial real estate transaction with a value in excess of the \$400,000 threshold is required to have an appraisal by a state-licensed or state-certified appraiser. Any commercial real estate transaction at or below the \$400,000 threshold requires an evaluation.

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<sup>74</sup> 5 U.S.C. 601 *et seq.*

<sup>75</sup> 13 CFR 121.201 (as amended, effective December 2, 2014).

<sup>76</sup> FDIC-supervised institutions are set forth in 12 U.S.C. 1813(q)(2).

<sup>77</sup> FDIC Call Report, March 31, 2017.

<sup>78</sup> The proposed definition of “Commercial Real Estate Transaction” would largely capture the following four categories of loans secured by real estate in the Call Report (FFIEC 031; RCFD 1410), namely loans that are: (1) for construction, land development, and other land loans; (2) secured by farmland; (3) secured by residential properties with five or more units; or (4) secured by nonfarm nonresidential properties. However, loans that provide both initial construction funding and permanent financing and are reported as construction, land development, and other land loans during the construction phase would be excluded from the definition.

To estimate the dollar volume of commercial real estate transactions the proposed change could potentially affect, the FDIC used information on the dollar volume and number of loans in the Call Report for small institutions from two categories of loans included in the definition of a commercial real estate transaction. The Call Report data reflect that 4.55 percent of the dollar volume of nonfarm, nonresidential loans secured by real estate has an original amount between \$1 and \$250,000, while 11.81 percent have an original amount between \$250,000 and \$1,000,000. The Call Report data also reflects that 8.85 percent of the dollar volume of agricultural loans secured by farmland has an original amount between \$1 and \$250,000, while 7.49 percent have an original amount between \$250,000 and \$500,000.<sup>79</sup> Assuming that the original amount of nonfarm, nonresidential loans secured by real estate and the original amount of agricultural loans secured by farmland are normally distributed, the FDIC estimates that 6.08 and 12.95 percent of loan volume is at or below the \$400,000 threshold for these categories, respectively.

Therefore, raising the appraisal threshold from \$250,000 to \$400,000 for commercial real estate transactions could affect an estimated 1.53 to 4.10 percent of the dollar volume of all commercial real estate transactions originated each year. This estimate assumes that the distribution of loans for the other loan categories within the proposed definition of commercial real estate transactions is similar to those loans secured by nonfarm, nonresidential properties or farmland.

The proposed rule is likely to reduce valuation review costs for covered institutions. The FDIC estimates that it takes a loan officer an average of 40 minutes to review an appraisal to ensure that it meets that standards set forth in Title XI, but 10 minutes to perform a similar

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<sup>79</sup> FDIC Call Report, March 31, 2017.

review of an evaluation, which does not need to meet the Title XI standards for appraisals. The proposed rule increases the number of commercial real estate transactions that would require an evaluation by raising the appraisal threshold from \$250,000 to \$400,000. Assuming that 15 percent of the outstanding balance of commercial real estate transactions for small entities gets renewed or replaced by new originations each year, the FDIC estimates that small entities originate \$31.9 billion in new commercial real estate transactions each year. Assuming that 1.53 to 4.10 percent of annual originations represent loans with an origination amount greater than \$250,000 but not more than \$400,000, the FDIC estimates that the proposed rule will affect approximately 1,504 to 4,040 loans per year,<sup>80</sup> or 0.5 to 1.33 loans on average for small FDIC-supervised institutions. Therefore, based on an estimated hourly rate, the proposed rule would reduce loan review costs for small entities by \$51,625 to \$138,673, on average, each year.<sup>81</sup> If lenders opt to not utilize an evaluation and require an appraisal on commercial real estate transaction greater than \$250,000 but not more than \$400,000 any reduction in costs would be smaller.

Any associated recordkeeping costs are unlikely to change for small FDIC-supervised entities as the amount of labor required to satisfy documentation requirements for an evaluation

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<sup>80</sup> Multiplying \$31.9 billion by 1.53 percent then dividing the product by an average loan amount of \$325,000 equals 1,504 loans and multiplying \$31.9 billion by 4.10 percent then dividing the product by an average loan amount of \$325,000 equals 4,040 loans.

<sup>81</sup> The FDIC estimates that the average hourly compensation for a loan officer is \$68.65 an hour. The hourly compensation estimate is based on published compensation rates for Credit Counselors and Loan Officers (\$43.40). The estimate includes the March 2017 75<sup>th</sup> percentile hourly wage rate reported by the BLS, National Industry-Specific Occupational Employment and Wage Estimates. The reported hourly wage rate is adjusted for changes in the CPI-U between May 2016 and March 2017 (1.83 percent) and grossed up by 155.3 percent to account for non-monetary compensation as reported by the March 2017 Employer Costs for Employee Compensation Data. Based on this estimate, loan review costs would decline between \$51,625 (1,504 loans multiplied by 30 minutes and multiplied by \$68.65 per hour) and \$138,673 (4,040 loans multiplied by 30 minutes and multiplied by \$68.65 per hour).

or an appraisal is estimated to be the same at about five minutes for either an appraisal or evaluation.

The proposed rule also is likely to reduce the loan origination costs associated with real estate appraisals for commercial real estate borrowers. The FDIC assumes that these costs are always paid by the borrower for this analysis. Anecdotal information from industry participants indicates that a commercial real estate appraisal costs between \$1,000 to over \$3,000, or about \$2,000 on average, and a commercial real estate evaluation costs between \$500 to over \$1,500, or about \$1,000 on average. Based on the prior assumptions, the FDIC estimates that the proposed rule will affect approximately 1,504 to 4,040 transactions per year<sup>82</sup>, or 0.5 to 1.33 loans on average for small FDIC-supervised institutions. Therefore, the proposed rule could reduce loan origination costs for borrowers doing business with small entities by \$1.5 to \$4.0 million on average per year.<sup>83</sup>

By lowering valuation costs on commercial real estate transactions greater than \$250,000 but less than or equal to \$400,000 for small FDIC-supervised institutions, the proposed rule could marginally increase lending activity. As discussed previously, commenters in the EGRPRA review noted that appraisals can be costly and time consuming. By enabling small FDIC-supervised institutions to utilize evaluations for more commercial real estate transactions, the proposed rule will reduce transaction costs. The reduction in loan origination fees could marginally increase commercial real estate lending activity for loans with an origination value greater than \$250,000 and not more than \$400,000.

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<sup>82</sup> Multiplying \$31.9 billion by 1.53 percent then dividing the product by an average loan amount of \$325,000 equals 1,504 loans and multiplying \$31.9 billion by 4.10 percent then dividing the product by an average loan amount of \$325,000 equals 4,040 loans.

<sup>83</sup> Multiplying 1,504 loans by \$1,000 savings equals \$1.5 million and multiplying 4,040 loans by \$1,000 savings equals \$4.0 million.

## ***B. Paperwork Reduction Act***

Certain provisions of the proposed rule contain “collection of information” requirements within the meaning of the Paperwork Reduction Act (PRA) of 1995.<sup>84</sup> In accordance with the requirements of the PRA, the agencies may not conduct or sponsor, and the respondent is not required to respond to, an information collection unless it displays a currently-valid Office of Management and Budget (OMB) control number. The OMB control number for the OCC is 1557-0190, the Board is 7100-0250, and the FDIC is 3064-0103, which would be extended, without revision. The agencies have concluded that the proposed rule does not contain any changes to the current information collections, however, the agencies are revising the methodology for calculating the burden estimates. The information collection requirements contained in this proposed rulemaking have been submitted by the OCC and FDIC to OMB for review and approval under section 3507(d) of the PRA<sup>85</sup> and section 1320.11 of the OMB’s implementing regulations.<sup>86</sup> The Board reviewed the proposed rule under the authority delegated to the Board by OMB.

### **Proposed Information Collection**

*Title of Information Collection:* Recordkeeping Requirements Associated with Real Estate Appraisals and Evaluations.

*Frequency of Response:* Event generated.

*Affected Public:* Businesses or other for-profit.

*Respondents:*

*OCC:* National banks, Federal savings associations.

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<sup>84</sup> 44 U.S.C. 3501-3521.

<sup>85</sup> 44 U.S.C. 3507(d).

<sup>86</sup> 5 CFR 1320.

*Board:* State member banks (SMBs) and nonbank subsidiaries of bank holding companies (BHCs).

*FDIC:* Insured state nonmember banks and state savings associations, insured state branches of foreign banks.

*General Description of Report:* For federally related transactions, Title XI requires regulated institutions<sup>87</sup> to obtain appraisals prepared in accordance with USPAP promulgated by the Appraisal Standards Board of the Appraisal Foundation. Generally, these standards include the methods and techniques used to estimate the market value of a property as well as the requirements for reporting such analysis and a market value conclusion in the appraisal. Regulated institutions are expected to maintain records that demonstrate that appraisals used in their real estate-related lending activities comply with these regulatory requirements. For commercial real estate transactions exempted from the Title XI appraisal requirements by the proposed rule, regulated institutions would still be required to obtain an evaluation to justify the transaction amount. The agencies estimate that the recordkeeping burden associated with evaluations would be the same as the recordkeeping burden associated with appraisals for such transactions.

*Current Action:* The threshold change in the proposed rule will result in lenders being able to use evaluations instead of appraisals for certain transactions. It is estimated that the time required to document the review of an appraisal or an evaluation is the same. While the rulemaking described in this proposed rule would not change the amount of time that institutions

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<sup>87</sup> National banks, Federal savings associations, State member banks (SMBs) and nonbank subsidiaries of bank holding companies (BHCs), Insured state nonmember banks and state savings associations, and insured state branches of foreign banks.

spend complying with the Title XI appraisal regulation, the agencies are using a more accurate methodology for calculating the burden of the information collections based on the experience of the agencies. Thus, the PRA burden estimates shown here are different from those previously reported. The agencies are (1) using the average number of loans per institution as the frequency and (2) using 5 minutes as the estimated time per response for the appraisals or evaluations.

### **PRA Burden Estimates**

*Estimated average time per response: 5 minutes.*

### **OCC**

*Number of Respondents: 1,284.*

*Annual Frequency: 1,488.*

*Total Estimated Annual Burden: 159,216 hours.*

### **Board**

*Number of Respondents: 828 SMBs; 1,215 nonbank subsidiaries of BHCs.*

*Annual Frequency: 419; 25.*

*Total Estimated Annual Burden: 28,911 hours; 2,531 hours.*

### **FDIC**

*Number of Respondents: 3,744.*

*Annual Frequency: 141.*

*Total Estimated Annual Burden: 43,992 hours.*

Comments are invited on:

(a) Whether the collections of information are necessary for the proper performance of the agencies' functions, including whether the information has practical utility;

- (b) The accuracy of the estimates of the burden of the information collections, including the validity of the methodology and assumptions used;
- (c) Ways to enhance the quality, utility, and clarity of the information to be collected;
- (d) Ways to minimize the burden of the information collections on respondents, including through the use of automated collection techniques or other forms of information technology; and
- (e) Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

All comments will become a matter of public record. Comments on aspects of this notice that may affect reporting, recordkeeping, or disclosure requirements and burden estimates should be sent to the addresses listed in the **ADDRESSES** section of this document. A copy of the comments may also be submitted to the OMB desk officer for the agencies: by mail to U.S. Office of Management and Budget, 725 17<sup>th</sup> Street NW, # 10235, Washington, DC 20503; by facsimile to (202) 395-5806; or by email to: [oir\\_submission@omb.eop.gov](mailto:oir_submission@omb.eop.gov), Attention, Federal Banking Agency Desk Officer.

### ***C. Riegle Act***

The Riegle Act requires that each of the agencies, in determining the effective date and administrative compliance requirements for new regulations that impose additional reporting, disclosure, or other requirements on IDIs, consider, consistent with principles of safety and soundness and the public interest, any administrative burdens that such regulations would place on depository institutions, including small depository institutions, and customers of depository

institutions, as well as the benefits of such regulations.<sup>88</sup> In addition, in order to provide an adequate transition period, new regulations that impose additional reporting, disclosures, or other new requirements on IDIs generally must take effect on the first day of a calendar quarter that begins on or after the date on which the regulations are published in final form.<sup>89</sup>

The proposed rule would reduce burden and would not impose any reporting, disclosure, or other new requirements on IDIs. For transactions exempted from the Title XI appraisal requirements by the proposed rule (*i.e.*, commercial real estate transactions between \$250,000 and \$400,000), lenders would be required to get an evaluation if they chose not to get an appraisal. However, the agencies do not view the option to obtain an evaluation instead of an appraisal as a new or additional requirement for purposes of the Riegle Act. First, the process of obtaining an evaluation is not new since IDIs already get evaluations for transactions at or below the current \$250,000-threshold. Second, for commercial real estate transactions between \$250,000 and \$400,000, IDIs could continue to get appraisals instead of evaluations. Because the proposed rule would impose no new requirements on IDIs, the agencies are not required by the Riegle Act to consider the administrative burdens and benefits of the rule or delay its effective date.

Because delaying the effective date of the rule is not required and would serve no purpose, the agencies propose to make the threshold increase effective on the first day after publication of the final rule in the Federal Register. Additionally, although not required by the Riegle Act, the agencies did consider the administrative costs and benefits of the rule while developing the proposal. In designing the scope of the threshold increase, the agencies chose to

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<sup>88</sup> 12 U.S.C. 4802(a).

<sup>89</sup> 12 U.S.C. 4802(b).

align the definition of commercial real estate transaction with industry practice, regulatory guidance, and the categories used in the Call Report in order to reduce the administrative burden of determining which transactions were exempted by the rule. The agencies also considered the cost savings that IDIs would experience by obtaining evaluations instead of appraisals and set the proposed threshold at a level designed to provide significant burden relief without sacrificing safety and soundness. The agencies note that comment on these matters has been solicited in questions 2 through 14 in in Section II, and in the RFA discussion in Section IV, of the **Supplementary Information**, and that the requirements of the Riegle Act will be considered as part of the overall rulemaking process. In addition, the agencies invite any other comments that further will inform the agencies' consideration of the Riegle Act.

#### *D. Solicitation of Comments on Use of Plain Language*

Section 722 of the Gramm-Leach-Bliley Act<sup>90</sup> requires the agencies to use plain language in all proposed and final rules published after January 1, 2000. Agencies invite comment on how to make these proposed rules easier to understand. For example:

- Have the agencies organized the material to suit your needs? If not, how could this material be better organized?
- Are the requirements in the proposed rules clearly stated? If not, how could the proposed rules be stated more clearly?
- Do the proposed rules contain language or jargon that is not clear? If so, which language requires clarification?

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<sup>90</sup> Pub. L. 106-102, section 722, 113 Stat. 1338 1471 (1999).

- Would a different format (grouping and order of sections, use of headings, paragraphing) make the proposed rules easier to understand? If so, what changes to the format would make the proposed rules easier to understand?
- What else could the agencies do to make the regulation easier to understand?

### ***E. Unfunded Mandates Act***

#### *OCC Unfunded Mandates Reform Act of 1995 Determination*

The OCC has analyzed the proposed rule under the factors in the Unfunded Mandates Reform Act of 1995 (UMRA) (2 U.S.C. 1532). Under this analysis, the OCC considered whether the proposed rule includes a Federal mandate that may result in the expenditure by state, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year (adjusted annually for inflation).

The proposed rule does not impose new requirements or include new mandates. Therefore, we conclude that the proposed rule will not result in an expenditure of \$100 million or more by state, local, and tribal governments, or by the private sector, in any one year.

### ***List of Subjects***

#### *12 CFR Part 34*

Appraisal, Appraiser, Banks, Banking, Consumer protection, Credit, Mortgages, National banks, Reporting and recordkeeping requirements, Savings associations, Truth in lending.

#### *12 CFR Part 225*

Administrative practice and procedure, Banks, banking, Federal Reserve System, Capital planning, Holding companies, Reporting and recordkeeping requirements, Securities, Stress testing

Banks, banking, Mortgages, Reporting and recordkeeping requirements, Savings associations.

**Office of the Comptroller of the Currency 12 CFR Part 34**

For the reasons set forth in the joint preamble, the OCC proposes to amend part 34 of chapter I of title 12 of the Code of Federal Regulations as follows:

**PART 34—REAL ESTATE LENDING AND APPRISALS**

1. The authority citation for part 34 continues to read as follows:

**Authority:** 12 U.S.C. 1, 25b, 29, 93a, 371, 1462a, 1463, 1464, 1465, 1701j-3, 1828(o), 3331 *et seq.*, 5101 *et seq.*, and 5412(b)(2)(B), and 15 U.S.C. 1639h.

2. Section 34.42 is amended by redesignating paragraphs (e) through (m) as paragraphs (f) through (n), respectively, and by adding a new paragraph (e) to read as follows:

**§ 34.42 Definitions.**

\* \* \* \* \*

(e) *Commercial real estate transaction* means a real estate-related financial transaction that is not secured by a 1-to-4 family residential property. A real estate-related financial transaction to finance the initial construction of a 1-to-4 family residential property that does not include permanent financing is a commercial real estate transaction.

\* \* \* \* \*

3. Section 34.43 is amended by:

- a. Removing the word “or” at the end of paragraph (a)(11);
- b. Revising paragraph (a)(12);
- c. Adding paragraph (a)(13); and
- d. Revising paragraphs (b) and (d)(2).

The revisions and addition read as follows:

**§ 34.43 Appraisals required; transactions requiring a State certified or licensed appraiser.**

(a) \* \* \*

(12) The OCC determines that the services of an appraiser are not necessary in order to protect Federal financial and public policy interests in real estate-related financial transactions or to protect the safety and soundness of the institution; or

(13) The transaction is a commercial real estate transaction that has a transaction value of \$400,000 or less.

(b) *Evaluations required.* For a transaction that does not require the services of a State certified or licensed appraiser under paragraph (a)(1), (a)(5), (a)(7), or (a)(13) of this section, the institution shall obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.

\* \* \*

(d) \* \* \*

(2) *Commercial real estate transactions of more than \$400,000.* All federally related transactions that are commercial real estate transactions having a transaction value of more than \$400,000 shall require an appraisal prepared by a State certified appraiser.

\* \* \* \* \*

**Federal Reserve Board**

**12 CFR Part 225**

For the reasons set forth in the joint preamble, the Board amends part 225 of chapter II of title 12 of the Code of Federal Regulations as follows:

**PART 225—BANK HOLDING COMPANIES AND CHANGE IN BANK CONTROL  
(REGULATION Y)**

1. The authority citation for part 225 continues to read as follows:

**Authority:** 12 U.S.C. 1817(j)(13), 1818, 1828(o), 1831i, 1831p-1, 1843(c)(8), 1844(b), 1972(l), 3106, 3108, 3310, 3331-3351, 3906, 3907, and 3909; 15 U.S.C. 1681s, 1681w, 6801 and 6805.

2. In Subpart G, section 225.62 is amended by redesignating paragraphs (e) through (m) as paragraphs (f) through (n), respectively, and by adding a new paragraph (e) to read as follows:

(e) *Commercial real estate transaction* means a real estate-related financial transaction that is not secured by a 1-to-4 family residential property. A real estate-related financial transaction to finance the initial construction of a 1-to-4 family residential property that does not include permanent financing is a commercial real estate transaction.

In Subpart G, section 225.63 is amended by:

- a. Removing the word “or” at the end of paragraph (a)(12);
- b. Revising paragraph (a)(13);
- c. Adding paragraph (a)(14);
- d. Revising paragraph (b); and
- e. Revising paragraph (d)(2).

The revisions and addition read as follows:

§ 225.63 Appraisals required; transactions requiring a State certified or licensed appraiser.

(a) \*\*\*

(13) The Board determines that the services of an appraiser are not necessary in order to protect Federal financial and public policy interests in real estate-related financial transactions or to protect the safety and soundness of the institution; or

(14) The transaction is a commercial real estate transaction that has a transaction value of \$400,000 or less.

(b) *Evaluations required.* For a transaction that does not require the services of a State certified or licensed appraiser under paragraph (a)(1), (a)(5), (a)(7), or (a)(14) of this section, the institution shall obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.

\*\*\*

(d) \*\*\*

(2) Commercial real estate transactions of more than \$400,000. All federally related transactions that are commercial real estate transactions having a transaction value of more than \$400,000 shall require an appraisal prepared by a State certified appraiser.

## **Federal Deposit Insurance Corporation**

### **12 CFR Part 323**

For the reasons set forth in the joint preamble, the FDIC amends part 323 of chapter III of title 12 of the Code of Federal Regulations as follows:

#### **PART 323—APPRAISALS**

1. Revise the authority citation for part 323 to read as follows:

**Authority:** 12 U.S.C. 1818, 1819 [“Seventh” and “Tenth”], 1831p-1 and 3331 *et seq.*

2. Revise the authority citation for subpart A of part 323 to read as follows:

**Authority:** This subpart is issued under 12 U.S.C. 1818, 1819 [“Seventh” and “Tenth”], 1831p-1 and title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (“FIRREA”) (Pub. L. 101--73, 103 Stat. 183, 12 U.S.C. 3331 et seq. (1989)).

3. In Subpart A, section 323.2 is amended by redesignating paragraphs (e) through (m) as paragraphs (f) through (n), respectively, and by adding a new paragraph (e) to read as follows:

(e) *Commercial real estate transaction* means a real estate-related financial transaction that is not secured by a 1-to-4 family residential property. A real estate-related financial transaction to finance the initial construction of a 1-to-4 family residential property that does not include permanent financing is a commercial real estate transaction.

4. In Subpart A, section 323.3 is amended by:

- a. Removing the word “or” at the end of paragraph (a)(11);
- b. Revising paragraph (a)(12);
- c. Adding paragraph (a)(13);
- d. Revising paragraph (b); and
- e. Revising paragraph (d)(2).

The revisions and addition read as follows:

**§ 323.3 Appraisals required; transactions requiring a State certified or licensed appraiser.**

(a) \*\*\*

(12) The FDIC determines that the services of an appraiser are not necessary in order to protect Federal financial and public policy interests in real estate-related financial transactions or to protect the safety and soundness of the institution; or

(13) The transaction is a commercial real estate transaction that has a transaction value of \$400,000 or less.

(b) *Evaluations required.* For a transaction that does not require the services of a State certified or licensed appraiser under paragraph (a)(1), (a)(5), (a)(7), or (a)(13) of this section, the institution shall obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.

\*\*\*

(d) \*\*\*

(2) *Commercial real estate transactions of more than \$400,000.* All federally related transactions that are commercial real estate transactions having a transaction value of more than \$400,000 shall require an appraisal prepared by a State certified appraiser.

Dated: [].

**Keith A. Noreika**

*Acting Comptroller of the Currency*

By order of the Board of Governors of the Federal Reserve System, [].

**Margaret McCloskey Shanks,**  
*Deputy Secretary of the Board.*

Dated at Washington, D.C. this [].

By order of the Board of Directors.

Federal Deposit Insurance Corporation.

**Robert E. Feldman,**

*Executive Secretary.*