

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. R-1568; RIN 7100 AE-81

FEDERAL DEPOSIT INSURANCE CORPORATION
12 CFR Part 323
RIN 3064 AE-56

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: Final rule.

SUMMARY: The OCC, Board, and FDIC (collectively, the agencies) are adopting a final rule to amend the agencies' regulations requiring appraisals of real estate for certain transactions. The final rule increases the threshold level at or below which appraisals are not required for commercial real estate transactions from \$250,000 to \$500,000. The final rule defines commercial real estate transaction as a real estate-related financial transaction that is not secured by a single 1-to-4 family residential property. It excludes all transactions secured by a single 1-to-4 family residential property, and thus construction loans secured by a single 1-to-4 family residential property are excluded. For commercial real estate transactions exempted from the appraisal requirement as a result of the revised threshold, regulated institutions must obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices.

DATES: *Effective date.* This final rule is effective on [INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER].

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SUPPLEMENTARY INFORMATION:

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[TBD]

I. Background and Summary of the Proposed Rule

In July 2017, the agencies invited comment on a notice of proposed rulemaking (proposal or proposed rule)¹ that would amend the agencies' appraisal regulations promulgated pursuant to Title XI of the Financial Institutions Reform, Recovery, and

¹ 82 FR 35478 (July 31, 2017).

Enforcement Act of 1989 (Title XI).² Specifically, the proposal would have increased the monetary threshold at or below which financial institutions that are regulated by the agencies (regulated institutions) would not be required to obtain appraisals in connection with commercial real estate transactions (commercial real estate appraisal threshold) from \$250,000 to \$400,000. The proposal followed the completion in early 2017 of the regulatory review process required by the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA).³ During the EGRPRA process, the agencies received numerous comments related to the Title XI appraisal regulations, including recommendations to increase the thresholds at or below which transactions are exempt from the Title XI appraisal requirements. Among other proposals developed through the EGRPRA process, the agencies recommended increasing the commercial real estate appraisal threshold to \$400,000.⁴

Title XI directs each federal financial institutions regulatory agency⁵ to publish appraisal regulations for federally related transactions within its jurisdiction. The purpose of Title XI is to protect federal financial and public policy interests⁶ in real estate-related transactions by requiring that real estate appraisals used in connection with federally related transactions (Title XI appraisals) be performed in accordance with

² 12 U.S.C. 3331 *et seq.*

³ Pub. L. 104–208, Div. A, Title II, section 2222, 110 Stat. 3009-414, (1996) (codified at 12 U.S.C. 3311).

⁴ See 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.

⁵ “Federal financial institutions regulatory agency” means the Board, the FDIC, the OCC, the National Credit Union Association (NCUA), and, formerly, the Office of Thrift Supervision. 12 U.S.C. 3350(6).

⁶ 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 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).

uniform standards, by individuals whose competency has been demonstrated, and whose professional conduct will be subject to effective supervision.⁷

Title XI directs the agencies to prescribe appropriate standards for Title XI appraisals under the agencies' respective jurisdictions,⁸ including, at a minimum, that appraisals be: (1) performed in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP);⁹ (2) written appraisals, as defined by the statute, by licensed or certified appraisers;¹⁰ 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.¹¹ A real estate-related financial transaction is defined as any transaction that involves: (i) the sale, lease, purchase, investment in or exchange of real 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.¹²

⁷ 12 U.S.C. 3331.

⁸ 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. See OCC: 12 CFR 34, subpart C; Board: 12 CFR 225.61(b); 12 CFR Part 208, subpart E; and FDIC: 12 CFR Part 323.

⁹ USPAP is written and interpreted by the Appraisal Standards Board of the Appraisal Foundation. 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-dbf4-41b3-9878-fac35923d2af.

¹⁰ Title XI defines "written appraisal" as "a written statement used in connection with a federally related transaction that is independently and impartially prepared by a licensed or certified appraiser setting forth an opinion of defined value of an adequately described property as of a specific date, supported by presentation and analysis of relevant market information. 12 U.S.C. 3350(10).

¹¹ 12 U.S.C. 3350(4).

¹² 12 U.S.C. 3350(5).

The agencies have authority to determine those real estate-related financial transactions that do not require the services of a state certified or state 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 do not require the services of an appraiser.¹³

The agencies have exempted several categories of real estate-related financial transactions from the Title XI appraisal requirements.¹⁴ The agencies have determined that these categories of transactions do not require appraisals by state certified or state 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 state 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.¹⁵ 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, established in 1994,¹⁶ all real estate-related financial transactions with a transaction value¹⁷ of \$250,000 or less, as well as certain real estate-secured business loans (qualifying business loans or QBLs) with a transaction value of \$1

¹³ See 59 FR 29482 (June 7, 1994).

¹⁴ See OCC: 12 CFR 34.43(a); Board: 12 CFR 225.63(a); and FDIC: 12 CFR 323.3(a).

¹⁵ Housing and Community Development Act of 1992, Pub. L. 102-550, section 954, 106 Stat. 3894 (amending 12 U.S.C. 3341).

¹⁶ See 59 FR at 29482. The NCUA has promulgated similar rules with similar thresholds. See 60 FR 51889 (October 4, 1995) and 66 FR 58656 (November 23, 2001).

¹⁷ 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 loan or the market value of each real property, respectively. See OCC: 12 CFR 34.42(m); Board: 12 CFR 225.62(m); and FDIC: 12 CFR 323.2(m).

million or less, do not require Title XI appraisals.¹⁸ QBLs are business loans¹⁹ 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.²⁰

For real estate-related financial transactions that are exempt from the Title XI appraisal requirement because they are at or below the applicable thresholds or qualify for the exemption for certain existing extensions of credit,²¹ the Title XI appraisal regulations require regulated institutions to obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices.²² An evaluation should contain sufficient information and analysis to support the financial institution's decision to engage in the transaction.²³

The agencies proposed to increase the commercial real estate appraisal threshold from \$250,000 to \$400,000. The proposal would have defined commercial real estate transaction to include all real estate-related financial transactions, except for those

¹⁸ See OCC: 12 CFR 34.43(a)(1) and (5); Board: 12 CFR 225.63(a)(1) and (5); and FDIC: 12 CFR 323.3(a)(1) and (5).

¹⁹ The Title XI appraisal regulations define "business loan" to mean "a loan or extension of credit to any corporation, general or limited partnership, business trust, joint venture, pool, syndicate, sole proprietorship, or other business entity." OCC: 12 CFR 34.42(d); Board: 12 CFR 225.62(d); and FDIC: 12 CFR 323.2(d).

²⁰ See OCC: 12 CFR 34.43(a)(5); Board: 12 CFR 225.63(a)(5); and FDIC: 12 CFR 323.3(a)(5).

²¹ 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 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); and FDIC: 12 CFR 323.3(a)(7) and (b).

²² See OCC: 12 CFR 34.43(b); Board: 12 CFR 225.63(b); and FDIC: 12 CFR 323.3(b).

²³ Evaluations are not required to be performed in accordance with USPAP or by state certified or state 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) and the *Interagency Advisory on the Use of Evaluations in Real Estate-Related Financial Transactions* (Evaluations Advisory, and together with the Guidelines, Evaluation Guidance). See, 75 FR 77450 (Dec. 10, 2010); OCC Bulletin 2016-8 (March 4, 2016); Board SR Letter 16-5 (March 4, 2016); and *Supervisory Expectations for Evaluations*, FDIC FIL-16-2016 (March 4, 2016).

secured by a 1-to-4 family residential property,²⁴ but including loans that finance the construction of 1-to-4 family properties and that do not include permanent financing.²⁵ Under the proposal, regulated institutions would have been required to obtain evaluations consistent with safe and sound banking practices in connection with commercial real estate transactions at or below the proposed \$400,000 threshold. The agencies did not propose increasing the thresholds for other types of real estate-related financial transactions, but solicited comment on the appropriateness of raising the threshold for residential real estate transactions and QBLs.

The comment period closed on September 29, 2017. The agencies collectively received over 200 comments from appraisers, appraiser trade organizations, financial institutions, financial institutions trade organizations, and individuals.

As noted in the proposal, increases in commercial property values over time have required regulated institutions to obtain Title XI appraisals for a larger proportion of commercial real estate transactions than in 1994 when the current \$250,000 threshold was established. This increase in the number of appraisals required may have contributed to increased burden for regulated institutions in terms of time and cost. The proposal was intended to reduce regulatory burden consistent with federal financial and public policy interests in real estate-related financial transactions. Based on supervisory experience and available data, the agencies published the proposal to accomplish these goals without posing a threat to the safety and soundness of financial institutions.

II. REVISIONS TO THE TITLE XI APPRAISAL REGULATIONS

Overview of Changes

After carefully considering the comments and conducting further analysis, the agencies are adopting a final rule that increases the commercial real estate appraisal

²⁴ 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; and FDIC: 12 CFR Part 365, Subpart A, Appendix A.

²⁵ The second part of the definition was intended to clarify, not be an exception to, the first part.

threshold with three modifications from the proposal. First, the agencies have decided to increase the commercial real estate appraisal threshold to \$500,000 rather than \$400,000 as proposed. Second, the final rule also makes a conforming change to the section requiring state certified appraisers to be used for federally related transactions that are commercial real estate transactions above the increased threshold.

Third, the final rule also reflects a change to the proposed definition of commercial real estate transaction, which no longer includes construction loans secured by a single 1-to-4 family residential property, regardless of whether the loan is for initial construction only or includes permanent financing. Thus, under the final rule, a loan that is secured by a single 1-to-4 family residential property, including a loan for construction, will remain subject to the \$250,000 threshold.²⁶ The Agencies made this change in the final rule after consideration of the comments, which suggested that including 1-to-4 family constructions loans that do not include permanent financing in the definition, but excluding those that do not, would not significantly reduce burden.

These changes are discussed in more detail below, in the order in which they appear in the rule. As described in more detail below, the effective date for the rule will be the date of its publication in the Federal Register. In the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act),²⁷ Congress amended the threshold provision to require “concurrence from the Consumer Financial Protection Bureau (CFPB) that such threshold level provides reasonable protection for consumers who purchase 1-4 unit single-family residences.”²⁸ The agencies have received concurrence from the CFPB that the commercial real estate appraisal threshold being adopted provides reasonable protection for consumers who purchase 1-4 unit single family residential properties.

²⁶ Residential construction loans secured by more than one 1-to-4 family residential property will be considered commercial real estate transactions subject to the higher threshold.

²⁷ Pub. L. 111–203, 124 Stat.1376.

²⁸ Dodd-Frank Act, § 1473, 124 Stat. 2190 (amending 12 U.S.C. 3341(b)).

Comments on the Proposed Increase to the Commercial Real Estate Appraisal Threshold

The agencies received a range of comments regarding the proposal to increase the commercial real estate appraisal threshold. Comments from financial institutions and financial institutions trade associations generally supporting an increase, although many requested a higher increase than proposed. Comments from appraisers and appraiser-related trade associations generally opposed an increase.

Commenters supporting a threshold increase stated that an increase would be appropriate, given the increases in real estate values since the current threshold was established, the cost and time savings to lenders and borrowers the higher threshold would provide, and the burden relief it would provide to financial institutions in rural and other areas where there are reported shortages of state licensed or state certified appraisers, which may have caused transaction delays and increased lending costs. Commenters supporting a threshold increase also asserted that it would provide burden relief for financial institutions, without sacrificing sound risk management principles or safe and sound banking practices, and that an increase would help justify the cost and return of originating smaller and less complex commercial real estate loans. Several commenters asserted the higher threshold could be implemented easily and would result in burden relief, for example, by reducing loan costs and minimizing delays in loan processing. One commenter asserted that the proposed increase would support local and regional economies, and another represented that it would assist small builders. This same commenter asserted that reducing burden on lenders would facilitate financing to builders generally, as they rely heavily on commercial banks for financing.

Commenters opposing an increase to the commercial real estate appraisal threshold asserted that an increase would elevate risks to financial institutions, the banking system, borrowers, small business owners, commercial property owners, and taxpayers. Several of these commenters asserted that the increased risk would not be justified by burden relief. Other commenters asserted that the proposed increase contradicts publicly stated concerns of the agencies relating to the state of the commercial real estate market and the quality of evaluation reports. Another commenter asserted that the inclusion of construction loans extended to consumers as commercial real estate

transactions would magnify risk, as the commenter viewed such loans as particularly risky. One commenter expressed concern that the proposal would lead to increased use of automated valuations, which the commenter asserted are not adequate substitutes for appraisals, or would eliminate collateral verifications altogether.

Some commenters opposing the threshold raised issues unrelated to risk. A few asserted that appraisals are relatively inexpensive and, thus, that the proposed increase would not materially reduce costs. One commenter expressed the view that an increase in the commercial real estate appraisal threshold would be contrary to consumer protection objectives. Another commenter asserted that the agencies are required by Title XI to receive concurrence from the CFPB for a threshold change. In support of its opposition to the proposal, a commenter cited a 2012 U.S. Government Accountability Office (GAO) report, contending that the report found no support for raising the threshold.²⁹ Another commenter asserted that the proposed threshold increase is contrary to Congressional intent and also asserted that most commenters during the EGRPRA process were against a threshold increase.

Several commenters rejected assertions that there was an appraiser shortage warranting regulatory relief, some asserting that any shortage is caused by appraisers' unwillingness to work for appraisal management companies (AMCs) at the reduced fees being offered to appraisers by AMCs. Two commenters questioned the impact of the proposed commercial real estate appraisal threshold on appraiser shortages, one asserting that the number of commercial real estate appraisers has remained relatively steady in recent years and the other asserting that appraiser shortages are primarily related to residential property valuations.

Many commenters opposing the proposal highlighted the benefits that state licensed or state certified appraisers bring to the process of valuing real estate collateral. One of these commenters asserted that appraisers serve a necessary function in real estate lending and expressed concerns that bypassing them to create a more streamlined valuation process could lead to fraud and another real estate crisis. Several commenters

²⁹ See GAO, "Real Estate Appraisals: Appraisal Subcommittee Needs to Improve Monitoring Procedures," GAO-12-147 (Jan. 2012).

highlighted that appraisers are the only unbiased party in the valuation process, in contrast to buyers, agents, lenders, and sellers, who each have an interest in the underlying transactions. One commenter asserted that appraisers have a unique vantage point during the property inspection process to provide lenders with information, in addition to a valuation, that may be critical to the lending decision and help to avoid bad loans and fraud.

Some commenters who were supportive of the proposal also discussed the role of appraisals and appraisers. One of these commenters asserted that appraisals are an integral part of the safety and soundness of the real estate industry, but believed that certain transactions are well served by alternative valuation methods. Some other commenters expressed skepticism about the value of appraisals prepared by independent appraisers. In this regard, one commenter asserted that banks have a better understanding of property values in their communities than appraisers from other areas, while another expressed concern for the reliability of appraisals and whether appraisers' valuations are keeping up with property growth trends. Another commenter expressed concern that appraisers' access to sales contracts can lead to an over-abundance of appraised values at or above the amounts in the contracts.

After carefully considering the comments received, the agencies have decided to increase the commercial real estate appraisal threshold. As discussed in the proposal and further detailed below, increasing the commercial real estate appraisal threshold will provide regulatory relief for financial institutions by removing the appraisal requirement for a material number of transactions without threatening the safety and soundness of financial institutions.

The agencies are increasing the threshold based on express statutory authority to do so if they determine in writing that the threshold does not represent a threat to the safety and soundness of financial institutions.³⁰ The agencies have made this safety and soundness determination and a detailed analysis is provided below.

Regarding consumer protection concerns, the agencies do not expect that this increase will affect a significant number of consumer transactions. As discussed in more

³⁰ 12 U.S.C. 3341(b).

detail below, the final rule is only raising the threshold for commercial real estate transactions. This definition was revised to exclude construction loans secured by a single 1-4 family residential property, which would have included construction loans to consumers. As a result of this change, the final rule will not affect a material number of consumer transactions.

Regarding the efficacy of Title XI appraisals, the agencies recognize and are supportive of the role that appraisers play in ensuring a safe and sound real estate lending process, regardless of whether it is in connection with an appraisal or an evaluation. Indeed, the Title XI appraisal regulations, appraiser independence requirements, and the Guidelines emphasize the importance of an independent opinion of collateral value in the process of real estate lending. Through the agencies' supervisory experience with loans that were exempted by the current thresholds and an analysis of loan losses over prior credit cycles for such loans, the agencies have found that evaluations can be an effective valuation method for lower-risk transactions. Even when the transaction amount is at or below the threshold, the Evaluation Guidance encourages regulated institutions to obtain Title XI appraisals when necessary for risk management and to preserve the safety and soundness of the institution.

A. Threshold Increase for Commercial Real Estate Transactions

Definition of Commercial Real Estate Transaction

The commercial real estate appraisal threshold increase applies only to transactions defined as "commercial real estate transactions." Under the proposed definition, a commercial real estate transaction would have included construction loans for 1-to-4 family residential units, but not those providing permanent financing. Accordingly, the proposed definition would have included a loan extended to finance the construction of a consumer's dwelling, but would have excluded construction loans that provide both the initial construction funding and permanent financing.

The agencies received several comments related to the proposed definition. Most comments were not supportive of the proposed treatment of loans to finance the construction of 1-to-4 family residential properties. The one commenter in support of the proposal to include 1-to-4 family construction-only loans in the definition of a

commercial real estate transaction asserted that these loans are underwritten similar to commercial real estate transactions.

Some commenters supported excluding all loans to finance the construction of 1-to-4 family residential properties from the definition. Some commenters maintained that it would be safer from a risk perspective to keep construction loans for 1-to-4 family properties in the residential loan category subject to the \$250,000 threshold. These commenters asserted that 1-to-4 family construction loans are riskier than conventional residential lending, and maintained that evaluations lack the market analysis needed for a phased construction project. One commenter asserted that there may be limited benefit to including transactions to finance the construction of 1-to-4 family residential properties without permanent financing in the definition of commercial real estate transaction, because an appraisal would be required prior to the permanent financing phase and prudent risk management would dictate obtaining the appraisal prior to initial funding. Another commenter asserted that the implementation of two thresholds for 1-to-4 family residential construction loans would cause confusion and increase regulatory burden on financial institutions.

A few commenters expressed the view that all residential construction loans should be included in the definition and subject to the higher threshold. One commenter noted that an increasing percentage of 1-to-4 family properties are rental properties and that the proposed definition would have excluded a class of rent-dependent real estate that should be classified as commercial real estate. Another commenter recommended that “construction-to-permanent” loans be included in the definition of commercial real estate transaction to increase the financing available for new home construction, indicating that strict underwriting and active engagement among the bank, home builder, and home buyer alleviate risks for these loans. This commenter supported subjecting all construction loans to the same treatment, and asserted that doing so would reduce regulatory burden, provide consistency, and allow for more efficient processes. Another commenter indicated that including all 1-to-4 family construction loans in the definition would avoid creating additional complications by distinguishing such loans into two different classes.

After carefully considering the comments, the agencies have adopted a definition of commercial real estate transaction that excludes construction loans secured by single 1-to-4 family residential properties. Specifically, the final rule defines commercial real estate transaction as a real estate-related financial transaction that is not secured by a single 1-to-4 family residential property. This definition eliminates the distinction between construction loans secured by a single 1-to-4 family residential property that only finance construction and those that provide both construction and permanent financing. Under the definition in the final rule, neither of these types of loans will be commercial real estate transactions; they will both remain subject to the \$250,000 threshold.

This approach addresses the potential confusion from subjecting two classes of construction loans secured by a single 1-to-4 family residential property to different threshold levels. The revised definition also reflects comments stating that Title XI appraisals are typically conducted for loans for construction of a single 1-to-4 family residential property regardless of whether the loan provides only financing for construction or provides “construction-to-permanent” financing.

The agencies have included the term “single” in the definition to clarify that only transactions secured by one 1-to-4 family residential property are excluded from the definition of “commercial real estate transaction,” whether financing construction or for other purposes. This change addresses potential confusion about whether a loan for the construction of multiple residential properties would meet the definition of “commercial real estate transaction;” a loan that is secured by multiple 1-to-4 family residential properties (for example, a loan to construct multiple properties in a residential neighborhood) would meet the definition of commercial real estate transaction and thus be subject to the higher threshold.

This approach addresses concerns about consumer protection, because a large portion of loans to finance the purchase or initial construction of a single 1-to-4 family residential property that are secured by the property are likely to be extended to consumers who will use the property as their dwelling. By contrast, transactions secured by multiple 1-to-4 family properties are more likely to be transactions to real estate developers or investors in rental properties.

The agencies note that they proposed to treat construction-only loans to consumers as commercial real estate transactions to maintain consistency with agency reporting standards and other regulations and guidance that address construction loans to consumers in other contexts. As in the proposal, the definition being adopted generally aligns with the categories of commercial real estate transactions under the Call Report³¹ and other agency guidance,³² with the exception that construction loans secured by a single 1-to-4 family property would not be considered a commercial real estate transaction for purposes of this rule.

The agencies have determined that, on balance, the benefits of adopting this definition of commercial real estate transaction outweigh the drawbacks of the limited inconsistency with other agency issuances relating to commercial real estate lending. Those issuances are for different purposes than the Title XI appraisal regulations, and a different set of considerations is relevant for determining what types of transactions are appropriately exempt from the Title XI appraisal requirement on the basis of transaction size. The definition of commercial real estate transaction in the final rule ensures that loans made to consumers are largely treated consistently, remaining subject to the

³¹ The following four categories of real-estate secured loans in the Consolidated Reports of Condition and Income (Call Report) (FFIEC 031; RCFD 1410) are largely captured in the definition of commercial real estate transaction in the rule: (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. As discussed in the proposal, loans that provide construction funding and are secured by a single 1-to-4 family residential property are typically reported as “for construction, land development, and other land loans”. The definition applies to corresponding categories of real estate-secured loans in the FFIEC 041 and FFIEC 051 forms of the Call Report.

³² Other interagency guidance includes all construction loans in one category: 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).

\$250,000 threshold. In addition, by categorizing residential construction loans more clearly, the definition of commercial real estate transaction being adopted can facilitate compliance and enhance the burden reduction benefits of the rule.

Threshold Increase

The agencies proposed increasing the commercial real estate appraisal threshold 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). As described in the proposal, the CRE Index³³ is a direct measure of the changes in commercial real estate prices in the United States.³⁴ The CRE Index is comprised of data from the CoStar Commercial Repeat Sale Index,³⁵ 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.³⁶ The data incorporated into this index covers

³³ 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>.

³⁴ 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>.

³⁵ 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. *Ibid.*

³⁶ 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>.

properties across the country and across all price ranges,³⁷ from before 1994 through the present.

According to the CRE Index, a commercial property that sold for \$250,000 as of June 30, 1994, would be expected to sell for approximately \$760,000 as of December 2016.³⁸ However, because the price of commercial real estate can be particularly volatile, the agencies proposed to base the increased threshold on the value of the CRE Index when commercial real estate prices were at their lowest point in the most recent downturn, which was \$423,000 in March 2010. The agencies invited comment on the proposed level for the commercial real estate appraisal threshold.

Most of the commenters, who supported increasing the threshold to at least \$400,000, supported a higher amount. Some of these commenters also advocated for automatically increasing or reevaluating the level more frequently than every ten years as real estate prices rise and valuation technology changes. Some commenters urged the agencies to conduct further analysis to determine whether the threshold could be increased to a higher amount, but did not specify an amount. Some commenters supported increasing the threshold to \$500,000 and suggested that this higher figure would avoid the need for additional changes to the threshold in the near-term due to expected increases in prices. A few commenters supported raising the threshold to \$750,000 or higher, claiming the methodology in the proposal was unnecessarily conservative.

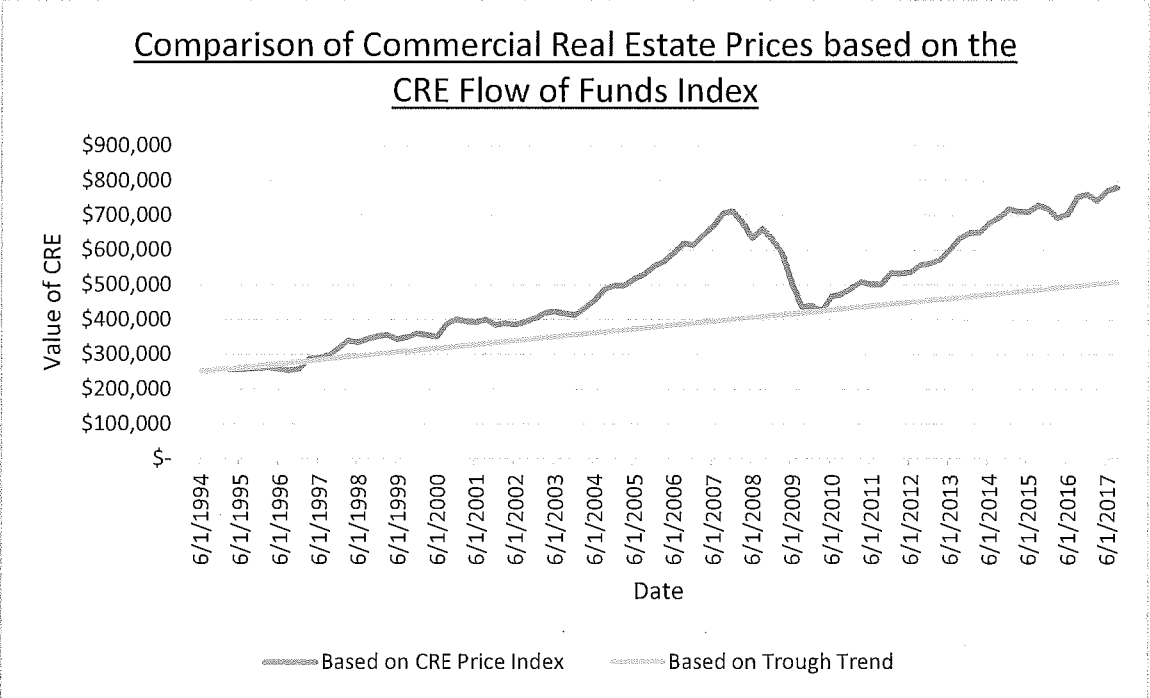
Some commenters supported lowering the commercial real estate appraisal threshold to unspecified amounts. Some of those commenters specifically objected to the methodology used by the agencies in the proposal, asserting that adjusting the previous \$250,000 level for changes in prices was inappropriate because that level was not itself the result of an inflation adjustment.

After careful consideration of the comments, the agencies have increased the commercial real estate appraisal threshold to \$500,000, rather than the proposed \$400,000 level. The proposed \$400,000 threshold was based on the value of the CRE

³⁷ See *id.*

³⁸ Since the proposal was published, the CRE Index data points for some of the recent quarters were revised. The numbers in this document reflect the revised CRE Index.

Index in March 2010, when commercial real estate prices were at their lowest point in the most recent downturn. The Agencies proposed this conservative approach, due to the volatility of commercial real estate prices over time. The agencies based the beginning point of this analysis on \$250,000, because supervisory experience with the \$250,000 threshold has confirmed that this threshold level did not threaten the safety and soundness of financial institutions. Based on the CRE Index, a commercial property that sold for \$250,000 as of June 30, 1994, would be expected to sell for \$423,600 in March 2010, which was the trough of the CRE price cycle. Following this trend, that property would be expected to have a conservative value of approximately \$509,000 as of December 2017 (as shown below). Based on the comments received and this further review of the CRE Index, as well as the safety and soundness analysis discussed below, the agencies have decided to finalize the threshold at \$500,000.



Regarding the suggestion to raise the commercial real estate appraisal threshold to \$750,000 or higher, the agencies also note that \$750,000 was close to the high point on the volatile CRE Index, as discussed above. Given the volatility in commercial real estate prices, raising the threshold to this amount or higher would raise safety and soundness concerns. Finally, a possible threshold increase to \$750,000 or higher may pose too great a risk to smaller institutions, as such transactions may represent a higher

percentage of capital for such firms than has historically been permitted under the 1994 threshold.

In the proposal, the agencies also invited comment on how having three threshold levels (\$250,000 for all transactions, \$400,000 for commercial real estate transactions, and \$1 million for QBLs) rather than the two threshold levels applicable to Title XI appraisals (\$1 million for QBLs and \$250,000 for all other transactions) would affect burden on regulated institutions. Three commenters supported the proposal, noting that having three thresholds would have minimal impact on operations. One commenter opposed having three thresholds, asserting that it will increase complexity, particularly for small community banks with less rigorous compliance operations. The agencies have determined that the burden reduction associated with a higher threshold for commercial real estate transactions outweighs the potential burden of implementing three thresholds.

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 a Title XI appraisal 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.³⁹ The analysis of supervisory experience and available data presented in the proposal indicated that the proposed threshold level of \$400,000 for commercial real estate transactions would not have posed a threat to the safety and soundness of financial institutions. The agencies invited comment on their preliminary finding and the data used. Taking into consideration those comments and updated analysis, discussed below, the agencies determine that the threshold level of \$500,000 for commercial real estate transactions does not pose a threat to the safety and soundness of financial institutions.

Multiple financial institutions trade associations, financial institutions, individuals, and home builder and realtor associations supported the agencies' analysis showing that an increase to the appraisal threshold for commercial real estate would not have a significant impact on the safety and soundness of financial institutions. A few commenters noted that appraisals are only one part of the underwriting process, one

³⁹ 12 U.S.C. 3341(b).

asserting that loans are primarily underwritten on borrowers' ability to repay, with collateral as a secondary consideration. Another commenter asserted that commercial borrowers tend to be larger entities, with the capital to withstand detrimental financial events and shifts in the market. This commenter also indicated that the proposal would not increase safety and soundness risk, given that the increased threshold would affect a relatively small number of transactions in the commercial real estate lending market.

Some commenters noted that evaluations would be required where appraisals were not obtained, and some asserted that the increased use of evaluations with these less complex loans would not increase risk if prepared with adequate analysis. One of these commenters asserted that evaluations for smaller transactions provide more targeted and precise data than appraisals performed by someone from another area.

The agencies received comments from appraisers, appraiser-related groups and individuals opposing the proposed increase, many of whom asserted that appraisals are key to preserving the safety and soundness of financial institutions and the economy. Several of these commenters claimed that evaluations were not an appropriate substitute for appraisals, some suggesting that they are less reliable and prepared by individuals that are not held to the same standards as appraisers. One commenter asserted that the increase would pose safety and soundness risks because commercial loans are riskier than residential loans. Another commenter suggested that entry-level properties that are lower in price and close to the threshold are more likely to have performance issues compared to more expensive properties. One commenter raised concerns that the rule focused on time and cost savings to financial institutions in selecting an appropriate valuation method, rather than risk.

Several commenters voiced concerns about recent price increases, increasing delinquencies, or volatility in the commercial real estate market, which, some asserted, may be indicative of a market "bubble." Some commenters suggested that it is the wrong time to relax valuation standards, given their view that past market bubbles have been preceded by loosening of underwriting and appraisal standards, and that poor valuation practices contributed to losses during past financial crises. One of these commenters asserted that there is increasing risk in commercial real estate lending, particularly among

smaller community and regional banks, which the commenter believed are less likely to have robust collateral risk management policies, practices and procedures.

Multiple commenters noted a 2015 appraiser trade association survey of appraisal industry professionals, including chief appraisers and appraisal managers at financial institutions, which showed that the majority of those surveyed opposed increasing the current \$250,000 threshold and believed that increases to the threshold could increase risk to lenders.

The agencies received a limited number of comments in response to the request for comment on the data sources used for the agencies' safety and soundness analysis from financial institutions, financial institution trade associations and appraiser trade associations. Multiple commenters asserted that the data in the proposal supports the increase in the commercial real estate threshold, and indicated that they did not know of other sources of data that the agencies should consider. A number of commenters asserted that the agencies' analysis was too conservative, that past housing crises do not imply current volatility, and that the data suggest the threshold could be increased further than proposed without threatening safety and soundness of financial institutions. One commenter opposing the proposal suggested that the data used in the agencies' safety and soundness analysis was weak and questioned why the agencies did not provide specific numbers to support the assertion that the data related to charge-offs from 2007-2012 is "no worse than" those from the years 1991-1994, except for marked increases in construction loan charge-offs.⁴⁰ This commenter also asserted that the agencies' analysis of the CoStar data should have considered that newly exempted loans under the higher threshold would more likely be extended to small businesses, which by nature are more vulnerable to market volatility and the potential for business failure.

⁴⁰ During the 1991-1994 credit cycle, the net charge-off rate for commercial real estate loans reached a high of about 4.5 percent. During the 2007-2012 credit cycle, net charge-off rates reached a high of about 3.5 percent. These are the numbers the agencies used to support their conclusion that the data related to charge-offs from 2007 to 2012 was no worse than that from the years 1991 to 1994. Federal Reserve Bank of San Francisco: Aggregate Net Charge-Off Rate Database as derived from the Federal Financial Institutions Examination Council Consolidated Reports of Condition and Income, FFIEC031 4Q 2016: <http://www.frbsf.org/banking/data/aggregate-data/>

Based on their supervisory experiences, the agencies disagree that increasing the commercial real estate appraisal threshold would increase risks to financial institutions, including smaller institutions. As outlined earlier, the agencies closely examined a variety of data and metrics indicating that the relative risks associated with the new threshold in terms of the scope of covered transactions were similar to those presented by the 1994 threshold. The agencies specifically examined the information from smaller insured depository institutions (IDIs) from Call Reports to assess the concentration risk for institutions and concluded that these risks were similar to those presented for larger IDIs. The agencies also note that smaller IDIs are often better positioned than larger institutions to understand and quantify local real estate market values since they serve a smaller, more defined market area.

Regarding comments concerning evaluations as a valuation method, in the agencies' views, evaluations are an effective valuation method for smaller commercial real estate transactions and other transactions under the thresholds. As provided in the Title XI appraisal regulations, evaluations for each transaction must be consistent with safe and sound banking practices. The Evaluation Guidance provides guidance on appropriate evaluation practices. In adopting the increased threshold for commercial real estate transactions, the agencies note that regulated institutions have the flexibility to choose to obtain a Title XI appraisal when markets are volatile or when an appraisal is warranted for other reasons.⁴¹

The agencies have no evidence that increasing the appraisal threshold to \$500,000 for commercial real estate transactions will materially increase the risk of loss to financial institutions. Analysis of supervisory experience concerning losses on commercial real estate transactions suggests that faulty valuations of the underlying real estate collateral since 1994 have not been a material cause of losses in connection with transactions at or below \$250,000.⁴² 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. Supervisory experience and an

⁴¹ 75 FR 77450, 77460.

⁴² See 82 FR at 35484.

examination of material loss reviews covering those decades suggest that larger acquisition, development, and construction transactions pose greater credit risk, 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.⁴³

In addition to considering the agencies’ supervisory experience since 1994, the agencies reviewed how the coverage of transactions exempted by the threshold would change, both in terms of number of transactions and aggregate value, in order to consider the potential impact on safety and soundness of increasing the commercial real estate appraisal threshold to \$500,000. In the proposal, the agencies used three different metrics to estimate the overall coverage of the existing threshold and the proposed threshold: (1) the number of commercial real estate transactions at or under the threshold as a share of the number of all commercial real estate transactions; (2) 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 (3) the dollar volume of commercial real estate transactions at or under the threshold relative to IDIs’ capital and the allowance for loan and lease losses, which act as buffers to absorb losses, as explained below. The agencies examined data reported on the Call Report and data from the CoStar Comps database to estimate the volume of commercial real estate transactions covered by the existing threshold and increased thresholds.

The Call Report data shows that the scope of the exemption in 1994, in terms of the number of transactions impacted, decreased significantly over time, and implies that raising the commercial real estate appraisal threshold to \$500,000 will not involve a greater number of transactions than when the thresholds were established in 1994.

Due to the manner in which IDIs report information on nonfarm nonresidential (NFNR) loans in the Call Report, this data set does not enable the agencies to calculate the percentage of loans that would fall under any threshold amount between \$250,000

⁴³ See id.

and \$1 million.⁴⁴ The percentage of the total dollar volume of loans that fall beneath the \$250,000 threshold is now less than a third of what it was when the threshold was established in 1994.⁴⁵ This is true even for institutions under \$1 billion in assets, who are more likely to hold smaller loans. Based in part on this analysis, the agencies conclude that the exposure of financial institutions will remain at acceptable levels with a \$500,000 commercial real estate appraisal threshold.

The CoStar Comps database provides sales value data on specific commercial real estate transactions and allows for an analysis of the estimated coverage at any potential threshold level. As described in the proposal, the agencies used this dataset to analyze the impact of increasing the commercial real estate appraisal threshold to \$400,000, and have recently updated this analysis to evaluate the impact of a \$500,000 threshold. An analysis of the CoStar Comps database for the most recent year available suggests that increasing the amount to \$500,000 would significantly increase the number of commercial real estate transactions exempted from the Title XI appraisal requirements, but the portion of the total dollar volume of commercial real estate transactions that would be exempted by the threshold would be comparatively minimal.

At the existing \$250,000 threshold and the proposed \$400,000 threshold, the percentage of commercial properties with loans in the CoStar Comps database that would be exempted from the Title XI appraisal regulations would have been 16.1 percent and 26.3 percent, respectively.⁴⁶ The \$500,000 threshold that the agencies are adopting will

⁴⁴ As described in the proposal, IDIs annually 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 million or less. They also annually report the dollar amount of all NFNR loans, including those over \$1 million. 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.

⁴⁵ In the proposal, the agencies explained that 18 percent of the dollar volume of all NFNR loans reported by IDIs had original loan amounts of \$250,000 or less when the current appraisal threshold was established in 1994, but 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. 82 FR at 35485.

⁴⁶ Certain percentages shown here differ from the values presented in the proposal because of ongoing refinements to the database and filters used to extract the information.

increase the percentage of transactions affected by another 5.5 percent, resulting in 31.9 percent of loans in the CoStar database being exempt from the appraisal requirement, or 15.7 percent more transactions than under the \$250,000 threshold. The proposed \$400,000 threshold would have increased the percentage of exempted transactions by dollar volume from 0.5 percent, under the current threshold, to 1.2 percent. Increasing the threshold to \$500,000 would increase the dollar volume by an additional 0.5 percent, so that a total of 1.8 percent of the dollar volume of loans in the CoStar database will be exempt from the appraisal requirement, or 1.3 percent more of the dollar volume than under the \$250,000 threshold. Thus, this analysis indicates that the increased threshold will affect a low aggregate dollar volume, but a material number of transactions.

The agencies have used this analysis and the Call Report analysis to determine that increasing the commercial real estate appraisal threshold to \$500,000 does not pose a threat to safety and soundness. In reaching this determination, the agencies also considered the fact that evaluations would be required for such transactions. The Guidelines provide regulated institutions with guidance on establishing parameters for ordering Title XI appraisals for transactions that present significant risk, even if those transactions are eligible for evaluations under the regulation.⁴⁷ Regulated institutions are encouraged to continue using a risk-focused approach when considering whether to order an appraisal for real estate-related financial transactions.

B. Use of Evaluations

Overview

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 commercial and residential real-estate related financial transactions of \$250,000 or less and QBLs with a

The methodology was further refined to improve its ability to reflect the relevant population of CRE transactions. Also, values presented here may not sum due to rounding.

⁴⁷ See Guidelines, Section XI.

transaction value of \$1 million or less.⁴⁸ Accordingly, the agencies proposed to require that regulated institutions entering into commercial real estate transactions at or below the proposed commercial real estate appraisal threshold obtain evaluations that are consistent with safe and sound banking practices unless the institution chooses to obtain an appraisal for such transactions.⁴⁹

The agencies are adopting this aspect of the proposal in the final rule without change.⁵⁰ An evaluation estimates the market value of real estate, but is not subject to the same requirements as a Title XI appraisal. For example, a Title XI appraisal must be performed by a state certified or state licensed appraiser and must conform to USPAP standards, whereas evaluations are not required to be performed by individuals with specific credentials or to conform to USPAP standards. As noted above, the agencies have issued guidance on the preparation of evaluations.⁵¹

The agencies requested comment on the proposed requirement that regulated institutions obtain evaluations for commercial real estate transactions at or below the proposed commercial real estate appraisal threshold. The agencies also asked related questions concerning whether additional guidance is needed by institutions to support the increased use of evaluations as well as questions concerning burden and costs related to the use of evaluations.

Evaluations Required at or Below the Threshold

Several commenters generally supported the proposal that regulated institutions obtain evaluations for commercial real estate transactions at or below the threshold. Other commenters expressed concern regarding the competency and credentialing of persons performing evaluations, as well as concerns regarding difficulty in locating

⁴⁸ See OCC: 12 CFR 34.43(a)(1) and (5); Board: 12 CFR 225.63(a)(1) and (5); and FDIC: 12 CFR 323.3(a)(1) and (5).

⁴⁹ An evaluation is not required when real estate-related financial transactions meet the threshold criteria and also qualify for another exemption from the appraisal requirements where no evaluation is required by the regulation.

⁵⁰ The agencies are adopting the commercial real estate appraisal threshold at \$500,000, which is higher than proposed. Financial institutions will be required to obtain evaluations for commercial real estate transactions with transaction values of \$500,000 or less.

⁵¹ See Evaluation Guidance.

persons qualified to perform evaluations.⁵² Some of these commenters also expressed concern over the lack of standards for evaluations and the lack of oversight and regulation for persons performing evaluations. One commenter urged the agencies to increase the qualification requirements for those completing evaluations if the commercial real estate appraisal threshold were increased.

As discussed in the proposal, institutions must obtain evaluations that are consistent with safe and sound banking practices. The agencies have provided guidance to regulated institutions on evaluations.⁵³ The Guidelines state that 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. An evaluation is not required to be completed by a state licensed or state certified appraiser, but may be completed by an employee of the regulated institution or by a third party, as addressed in the Evaluations Advisory.⁵⁴ However, the agencies' final rule does not prohibit regulated institutions from using state licensed or state certified appraisers to prepare evaluations. A Title XI appraisal would satisfy the requirement for an "appropriate evaluation of real property collateral that is consistent with safe and sound banking practices;" thus, regulated institutions that choose to obtain Title XI appraisals for real estate-related financial transactions that require evaluations are not in violation of the Title XI appraisal regulations.

Evaluation Guidance

The agencies also requested comment on the type of additional guidance, if any, regulated institutions need to support the increased use of evaluations. In response, the agencies received comments indicating concern regarding the clarity of, and the burden

⁵² A commenter highlighted two sentences in the proposal that appeared to conflict with the requirements of the appraisal regulations. First, the commenter disagreed with the following statement in the proposal: "Unlike appraisals, evaluations may be performed by a lender's own employees and are not required to comply with USPAP." The agencies agree with the commenter that regulations do not prohibit employees of regulated institutions from preparing appraisals if they are so qualified and independent of the real estate-related financial transaction.

⁵³ See Evaluation Guidance.

⁵⁴ OCC Bulletin 2016-8 (March 4, 2016); Board SR Letter 16-05 (March 4, 2016); and *Supervisory Expectations for Evaluations*, FDIC FIL-16-2016 (March 4, 2016).

produced by, the existing guidance on evaluations. A few commenters requested that the agencies provide additional guidance, such as guidance relating to the adequacy of evaluation products available on the market or examples of acceptable industry practices for evaluations. Some other commenters requested that the agencies revisit and relax the current guidance pertaining to evaluations and ensure examiners accept evaluations when permissible. One commenter expressed the view that a simplification would make the current existing guidance for evaluations less time consuming and complex for lower value transactions. Another commenter suggested there should be no need for a review of internal evaluations where the direct lender did not complete the evaluation.

The Evaluation Guidance provides information to help ensure that evaluations provide a credible estimate of the market value of the property pledged as collateral for the loan. The current Evaluation Guidance provides flexibility to regulated institutions for developing evaluations that are appropriate for the type and risk of the real estate financial transaction and does not prescribe specific valuation approaches or products to use tools in the development of evaluations. Also, in addition to various valuation approaches, the Guidelines discuss the possible use of several analytical methods and technological tools in the development of evaluations, such as automated valuation models and tax assessment values. The agencies will continue to assess the adequacy of agency guidance on evaluations.

Cost and Burden of Evaluations

The agencies invited comment regarding whether the use of evaluations reduces burden and cost as compared to the use of Title XI appraisals. The agencies also invited comment on whether evaluations are currently prepared by in-house staff or outsourced to appraisers or other qualified professionals.

The agencies received several comments indicating that the proposed increase in the commercial real estate appraisal threshold and the increased use of evaluations would provide cost and time savings for consumers and institutions, because evaluations tend to cost less than appraisals and take less time to prepare. One commenter asserted that third party evaluations are approximately 25 percent of the cost of an appraisal. Another commenter indicated that some financial institutions prefer to conduct them in-house to maintain consistency of the product and because of staff knowledge of the

marketplace. One commenter asserted that appraiser-developed evaluations are unnecessarily expensive, necessitating evaluations to be conducted in-house. Another commenter indicated that increasing the threshold would provide cost savings for portfolio loans but would not address issues related to secondary market requirements, which are outside the agencies' purview.

On the other hand, some commenters asserted that the agencies had overstated how much the proposal would reduce burden for regulated institutions, and questioned the agencies' methods for estimating the reduction in burden. Some commenters expressed concern regarding the length of time required to review an evaluation. A few commenters suggested that the agencies' cost analysis reflected a lack of precision and absence of detailed research to determine the cost differential of appraisals and evaluations between the current and proposed threshold. This same commenter asserted that evaluations lack the detail of appraisals, and, as a result, lenders are often required to perform additional research in determining whether evaluations are credible, which reduces cost and time savings produced by the proposal. One commenter implied that the limited guidance for performing evaluations creates confusion, which results in added costs. One commenter asserted that it is not true that evaluations contain less detailed information or take less time to review than appraisals.⁵⁵ Another commenter asserted that, because evaluations provide less detail than appraisals, lenders may be required to do more research to determine whether the value conclusion is credible.

The agencies carefully considered these comments in evaluating the rule's impact on the time to obtain and review Title XI appraisals and evaluations. The agencies conclude that there may be less delay in finding appropriate personnel to perform an evaluation than to perform a Title XI appraisal, particularly in rural areas, because

⁵⁵ Two commenters disagreed with the agencies' use of the term "loan officer" relative to the estimated time for reviewing an appraisal or evaluation, and asserted that the usage of the term could be perceived to imply that originators are permitted to be involved in the appraisal review process, which is contrary to the agencies' appraiser independence requirements. The agencies were using the term "loan officer" in its broadest context, and did not intend to imply that the officer originating the credit may conduct appraisal or evaluation reviews relating to that credit. The use of the term "loan officer" was not intended to change standards established on appraiser independence or any implementing guidance.

evaluations are not required to be prepared by a certified or licensed appraiser. Requiring regulated institutions to procure the services of a state licensed or state certified appraiser to prepare evaluations for commercial real estate transactions at or below the threshold could impose significant additional costs on lenders and borrowers without materially increasing the safety and soundness of the transactions. The agencies' data and analysis reflect that the increase in the commercial real estate appraisal threshold and corresponding increased use of evaluations could result in a cost savings of several hundred dollars for each commercial real estate transaction, as discussed below.

Based on supervisory experience the agencies conclude that regulated institutions generally need less time to review evaluations than Title XI appraisals, because the content of the report can be less comprehensive than an appraisal report. Transactions permitting the use of an evaluation typically have a lower dollar value, often are less complex, or are subsequent to previous transactions for which Title XI appraisals were obtained. Therefore, a consolidated analysis is more likely to be used in an evaluation. The agencies estimate that, on average, the time to review an evaluation for an affected transaction under the final rule will be approximately 30 minutes less than the time to review an appraisal.⁵⁶

In evaluating this rule, the agencies considered the impact of obtaining evaluations instead of Title XI appraisals on regulated institutions and borrowers. As noted in the proposal, 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 \$500,000, 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

⁵⁶ The agencies recognize some evaluations take longer to review than some appraisals; yet, on average, evaluations are likely to take less time to review than appraisals. This view is based on supervisory experience as well as discussions with regulated institutions.

per transaction affected by the proposal. Comments from financial institutions generally affirmed similar information presented in the proposal.

In considering the aggregate effect of this rule, the agencies considered the number of transactions affected by the increased threshold. 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 16 percent under the rule. Thus, while the precise number of affected transactions and the precise cost reduction per transaction cannot be determined, the rule is expected to lead to significant cost savings for regulated institutions that engage in commercial real estate lending.

Competitive Disadvantage of Evaluations

The agencies received comments from financial institutions, individuals, and a trade association representing valuation professionals, indicating concern that the proposal would put smaller banks that do not have in-house expertise to prepare evaluations at a competitive disadvantage to larger banks. Commenters asserted that these banks hire outside parties to prepare evaluations and pass the cost along to borrowers, making their loans more expensive than comparable loans at larger financial institutions.

In evaluating the final rule, the agencies considered these concerns. In response, the agencies note that the cost for completing an evaluation would be less than the cost for completing a Title XI appraisal for the same property, which thereby reduces burden. The goal of the agencies with this increase is to provide flexibility to regulated institutions in approaching property valuation. Some institutions may not currently be in a position to take advantage of this flexibility. However, raising the threshold will help those regulated institutions that choose to train in-house staff to perform evaluations and would reduce costs for those institutions that choose to outsource evaluations.

C. State Certified Appraiser Required

As described in the proposal, 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.”⁵⁷ In order to make this paragraph consistent with the other proposed changes to the appraisal regulations, the agencies proposed to change its wording to introduce the \$400,000 threshold and use the term “commercial real estate transaction.” The agencies did not receive any comments on this proposed change.

Given the change from the proposed rule from a \$400,000 threshold to a \$500,000 threshold, the final rule makes a corresponding change to this section. The amendment to this provision is a technical change that does not alter any substantive requirement.

III. EFFECTIVE DATE

The agencies proposed to make the final rule, if adopted, effective upon publication in the Federal Register. The agencies reasoned that a delayed effective date was not required by applicable law because the proposal exempted additional transactions from the Title XI appraisal requirements and did not impose any new requirements on regulated institutions.⁵⁸ The agencies requested comment on whether the proposed effective date was appropriate.

The agencies received three comments on the proposed effective date. One commenter supported the proposed effective date and did not think it would pose challenges to financial institutions. The other two commenters disagreed with an immediate effective date, asserting that financial institutions required time to adjust policies and procedures to implement the proposed changes. One commenter recommended a six-month to one-year implementation period, while the other suggested an effective date 180 days after the final rule is published.

The agencies have retained the proposed effective date, which is the date of publication in the Federal Register.⁵⁹ In doing so, the agencies balanced the need for

⁵⁷ OCC: 12 CFR 34.43(d); Board: 12 CFR 225.63(d)(2); and FDIC: 12 CFR 323.3(d)(2).

⁵⁸ See 82 FR at 35482.

⁵⁹ As discussed in Section V.A of the **Supplementary Information**, 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. Additionally, 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

some financial institutions to update policies and procedures to incorporate evaluations for transactions exempted by the revised threshold with the benefit of an immediate effective date, which will enable institutions to benefit from lower costs and regulatory relief upon or shortly after the effective date of the final rule. The agencies note that an effective date immediately upon publication in the Federal Register is the approach used in adopting the 1994 amendments to the Title XI appraisal regulations. The agencies are not aware of any evidence that using an immediate effective date in connection with the 1994 amendments caused a competitive disadvantage or hardship to regulated institutions. The agencies also note that regulated institutions have the discretion to use Title XI appraisals in lieu of evaluations for any exempt transaction.

IV. OTHER EFFORTS TO RELIEVE BURDEN

Residential and Qualifying Business Loan Thresholds

The agencies explained in the proposal that they were not proposing any threshold increases for transactions secured by a single 1-to-4 family residential property (residential transactions) or QBLs in connection with this rulemaking. The agencies requested comment on whether there are other factors that should be considered in evaluating the current appraisal threshold for residential transactions. The agencies also invited comment and supporting data on the appropriateness of raising the current \$1 million threshold for QBLs and posed a number of specific questions related to regulated institutions' experiences with QBLs.

Numerous commenters, particularly financial institutions and their trade associations, encouraged the agencies to consider increasing the threshold for residential transactions, though few introduced new factors for the agencies' consideration. Many of these commenters asserted that an increase would produce cost and time savings that would benefit regulated institutions and consumers without threatening the safety and soundness of financial institutions. In support of its position that an increase would not

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 V.D of the **Supplementary Information**, the final rule does not impose any new requirements on IDIs, and, as such, the effective date requirement of the Riegle Act is inapplicable.

threaten safety and soundness, one of these commenters asserted that there is less risk in the homogenous loan pool of 1-to-4 family residential loans than there is in commercial real estate. One commenter asserted that the consumer benefits of appraisals have been overstated, that appraisals are primarily for the benefit of financial institutions, and that consumers could always order their own appraisals.

Several commenters supporting an increase in the threshold for residential transactions noted that an increase in the threshold would be justified by increases in residential property values since the current threshold was established. Some commenters represented that relief would be particularly beneficial for lending in rural communities that often have shortages in state licensed and state certified appraisers. One of these commenters cited feedback from several state bank supervisory agencies indicating that access to appraisers, particularly for residential transactions, is limited in rural areas within their states and that federal appraisal regulations are causing significant burden. A few commenters noted that the Government Sponsored Enterprises (GSEs) waive appraisal requirements for certain residential mortgage loans that they purchase and they expected the GSEs to expand eligibility for such waivers. In this regard, they asserted that increasing the threshold in the appraisal regulations would provide burden relief. One of these commenters asserted that as the GSEs expand their appraisal waiver programs, regulated institutions that hold residential mortgage loans in portfolio will be at a competitive disadvantage if the current threshold in the appraisal regulations is not increased. Another commenter asserted that, even if inconsistent GSE requirements would negate some of the burden reduction, the agencies should raise the residential threshold now if, by doing so, safety and soundness would not be jeopardized. A separate commenter suggested that the agencies should provide a *de minimis* exemption from appraisal requirements for residential mortgage loans that are retained in portfolio by regulated institutions. This same commenter urged the agencies to consider more regional data in deciding whether to make future changes to the threshold for residential transactions.

Many commenters, particularly appraisers and appraiser trade associations, supported with the agencies' decision not to propose an increase in the threshold for residential transactions. Several commenters pointed to the safety and soundness and

consumer protection benefits of obtaining appraisals in connection with residential transactions. Several commenters also asserted that the appraisal regulations already exempt a significant percentage of residential mortgage loans. One commenter suggested that the agencies should not rely on policies of other federal entities, such as the GSEs, in making decisions about the appraisal regulations. Another commenter expressed concern that the potential negative consequences of raising the threshold could be exacerbated by the loosening of appraisal standards by the GSEs for some transactions. Another commenter asserted that increasing the threshold for residential transactions could discourage entrance into the appraisal profession and cause further appraiser shortages.

Regarding an increase to the appraisal threshold for QBLs, the majority of comments received opposed an increase. These commenters, who were appraisers or their trade associations, cautioned against a loosening of standards that could raise safety and soundness concerns. Commenters supporting an increase in the QBL threshold asserted that the value of real estate offered as collateral on a QBL is a secondary consideration, because the primary source of repayment is not the income from or sale of that collateral. Some commenters also supported an increase in the threshold due to limited availability of appraisers in their states. Commenters advocated a range of increases from \$1.5 million to \$3 million.

Few commenters specifically addressed the agencies' questions regarding unique risks that may be posed by QBLs, data regarding QBLs, and regulated institutions' experiences in applying the current QBL threshold. Regarding risks posed by QBLs, one financial institutions trade association commented that its members consider QBLs to be higher-risk loans. An appraiser trade association that was opposed to an increase asserted that small business loans are riskier than others and that lenders with concentrations in such loans are at greater risk. The commenter also noted that such loans are usually held in portfolio, thus increasing risk. Regarding the agencies' requests for data on QBLs, a commenter expressed surprise that the agencies lack data on QBL concentrations, and asserted this lack of data further supports not increasing the threshold. In response to the agencies' question regarding regulated institutions' experiences in applying the QBL threshold, a commenter asserted that many loan officers are poorly trained in classifying loans as either real estate or business. The commenter recommended that the agencies

provide examples of these types of loans. In addition, two commenters asked the agencies to clarify the QBL threshold relative to transactions secured by farmland.

The agencies appreciate the issues raised by the commenters relating to the thresholds for residential transactions and QBLs. As discussed in the proposal, the agencies decided not to propose any change to these thresholds in connection with this rulemaking. Nevertheless, the comments reflect a variety of issues that the agencies would consider if they decide to propose changes to the residential or QBL thresholds in the future.

Regarding the requests for clarification of the QBL threshold, the Title XI appraisal regulations have established a \$1 million threshold that is applicable to any business loans that are not dependent on the sale of, or rental income derived from, real estate as the primary source of repayment.⁶⁰ For example, a loan secured by a farm, which could include a situation where one or more affiliated limited liability companies own the farmland securing the loan, could be treated as a QBL subject to the \$1 million threshold, if repayment is primarily from the proceeds from the farm business (*e.g.*, sale of crops and related payments). However, a real estate-related financial transaction secured by farmland whose repayment is primarily from rental income from renting or leasing the farmland to a non-affiliated entity would be subject to the final rule's \$500,000 threshold.

Other proposals and clarifications

The agencies received several comments suggesting additional ways the agencies could reduce burden under the Title XI appraisal regulations. One commenter urged the agencies to review the appraisal requirements of other federal agencies and pursue ways to make appraisal requirements across agencies more consistent. The agencies have publically articulated their interest in seeking ways to coordinate appraisal standards across various government agencies that are involved in residential mortgage lending.⁶¹

⁶⁰ See OCC: 12 CFR 34.43(a)(5); Board: 12 CFR 225.63(a)(5); and FDIC: 12 CFR 323.3(a)(5).

⁶¹ See EGRPRA Report at 36; 82 FR at 35482.

The agencies have begun conducting outreach to government agencies to implement this goal and will continue to consider opportunities to do so.

Another commenter asserted that the agencies should focus on allowing the use by appraisers of products that streamline the valuation process, instead of exempting additional transactions from the appraisal requirements. Several commenters, including a financial institution and a financial institutions trade association, suggested that certain transactions could be added to the list of exemptions from the appraisal requirements to further reduce regulatory burden without sacrificing safety and soundness. These suggestions included exemptions for transactions secured by real estate outside the United States; loans below a threshold that a bank originates and retains “in-house;” transactions involving mortgage backed securities and pools of mortgages; and loans made to certain community development organizations. An association of state bank supervisors requested that the agencies release further guidance on the Title XI process for temporary waivers of appraiser certification and licensing requirements and also requested that the education requirements for appraiser qualifications be relaxed. A financial institution suggested establishing an additional threshold of \$50,000, below which certain transactions would not require appraisals or evaluations.

These comments concerning additional potential exemptions from the appraisal regulations and additional burden relieving measures are outside the scope of this rulemaking. However, the agencies appreciate the suggestions for ways to expand burden relief beyond what was proposed.

V. REGULATORY ANALYSIS

A. Waiver of Delayed Effective Date

This final rule is effective on [INSERT DATE PUBLISHED IN THE FEDERAL REGISTER]. The 30-day delayed effective date required under the APA is waived pursuant to 5 U.S.C. 553(d)(1), which provides for waiver when a substantive rule grants or recognizes an exemption or relieves a restriction. The amendment adopted in this final rule exempts additional transactions from the Title XI appraisal requirements, which has the effect of relieving restrictions. Consequently, the amendment in this final rule meets the requirements for waiver set forth in the APA.

B. 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 commercial real estate loans in amounts that fall between the current and final thresholds. Therefore, we cannot estimate how many small entities may be affected by the increase threshold. However, because the final rule does not contain any new recordkeeping, reporting, or compliance requirements, the final rule will not impose costs on any OCC-supervised institutions. Accordingly, the OCC certifies that the final rule will not have a significant economic impact on a substantial number of small entities.

Board: The Board is providing a regulatory flexibility analysis with respect to this final rule. The RFA requires that an agency prepare and make available a final regulatory flexibility analysis in connection with a final rulemaking that the agency expects will have a significant economic impact on a substantial number of small entities. The commercial real estate appraisal threshold increase applies to certain IDIs and non-bank entities that make loans secured by commercial real estate.⁶² The SBA establishes size standards that define which entities are small businesses for purposes of the RFA.⁶³

⁶² For its RFA analysis, the Board considered all Board-regulated creditors to which the proposed rule would apply.

⁶³ 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.

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 final rule.⁶⁴ Based on the Board's analysis, and for the reasons discussed below, the final rule may have a significant positive economic impact on a substantial number of small entities.

The Board requested comment on all aspects of the initial regulatory flexibility analysis it provided in connection with the proposal. The comments received are addressed below.

A. Reasons for the Threshold Increase

In response to comments received in the EGRPRA process and in connection with the proposal, the agencies are increasing the commercial real estate appraisal threshold from \$250,000 to \$500,000. Because commercial real estate prices have increased since 1994, when the current \$250,000 threshold was established, a smaller percentage 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 the safety and soundness of financial institutions.

B. Statement of Objectives and Legal Basis

As discussed above, the agencies' objective in finalizing 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 CFPB that such threshold level provides

⁶⁴ Asset size and annual revenues are calculated according to SBA regulations. See 13 CFR 121 et seq.

reasonable protection for consumers who purchase 1-to-4 unit single-family homes.⁶⁵ Based on available data and supervisory experience, the agencies tailored the size and scope of the threshold increase to ensure that it would not pose a threat to the safety and soundness of financial institutions or erode protections for consumers who purchase 1-to-4 unit single-family homes.

The Board's final rule applies 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 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 will be affected by the final rule because the number of small entities that will engage in commercial real estate transactions at or below the commercial real estate appraisal threshold is unknown.

C. Projected Reporting, Recordkeeping and Other Compliance Requirements

The final rule would reduce reporting, recordkeeping, and other compliance requirements for small entities. For transactions at or below the threshold, regulated institutions will be given the option to obtain an evaluation of the property instead of an appraisal. 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.

⁶⁵ 12 U.S.C. 3341(b).

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 evaluation takes approximately 30 minutes less to review than an appraisal. Thus, the agencies believe that final rule will alleviate approximately 30 minutes of employee time per affected transaction for which the lender obtains an evaluation instead of an appraisal. As discussed above, some commenters provided anecdotal evidence to show that the agencies' estimate of time savings was incorrect. The agencies recognize that certain evaluations may take longer to review than others; however, this variation was taken into account in the agencies' estimate of the average time savings that are expected to occur.

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 16 percent under the final 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 final 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 final rule.

E. Discussion of Significant Alternatives

The agencies considered additional burden-reducing measures, such as increasing the commercial threshold to an amount higher than \$500,000 and increasing the residential and business loan thresholds, but did not implement such measures for the safety and soundness and consumer protection reasons discussed in the proposal. For transactions exempted from the Title XI appraisal requirements under the commercial real estate appraisal threshold, the final rule requires regulated institutions to get an evaluation if they do not choose to obtain a Title XI 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 appraisal 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 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.⁶⁶ 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.⁶⁷ 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 3,675 depository institutions,⁶⁸ of which 2,950 are defined as small banking entities by the terms of the RFA.⁶⁹ According to the Call Report 2,950 small entities reported holding some volume of real estate related financial transactions that meet the final rule’s definition of a commercial real estate transaction.⁷⁰ Therefore, 2,950 small entities could be affected by the final rule.

The final rule will raise the appraisal threshold for commercial real estate transactions from \$250,000 to \$500,000. Any commercial real estate transaction with a value in excess of the \$500,000 threshold is required to have an appraisal by a state-licensed or state-certified appraiser. Any commercial real estate transaction at or below the \$500,000 threshold requires an evaluation.

⁶⁶ 5 U.S.C. 601 et seq.

⁶⁷ 13 CFR 121.201 (as amended, effective December 2, 2014).

⁶⁸ FDIC-supervised institutions are set forth in 12 U.S.C. 1813(q)(2).

⁶⁹ FDIC Call Report, September 30, 2017.

⁷⁰ The 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 secured by a single 1-to-4 family residential property would be excluded from the definition. The definition applies to corresponding categories of real estate-secured loans in the FFIEC 041 and FFIEC 051 forms of the Call Report.

To estimate the dollar volume of commercial real estate transactions the 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 3.92 percent of the dollar volume of nonfarm, nonresidential loans secured by real estate has an original amount between \$1 and \$250,000, while 10.19 percent have an original amount between \$250,000 and \$1 million. The Call Report data also reflects that 7.30 percent of the dollar volume of agricultural loans secured by farmland has an original amount between \$1 and \$250,000, while 6.05 percent have an original amount between \$250,000 and \$500,000.⁷¹ 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 6.28 and 13.35 percent of loan volume is at or below the \$500,000 threshold for these categories, respectively.

Therefore, raising the appraisal threshold from \$250,000 to \$500,000 for commercial real estate transactions could affect an estimated 2.36 to 6.05 percent of the dollar volume of all commercial real estate transactions originated each year for small FDIC-supervised institutions. This estimate assumes that the distribution of loans for the other loan categories within the definition of commercial real estate transactions is similar to those loans secured by nonfarm, nonresidential properties or farmland.

The final 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 review of an evaluation, which does not need to meet the Title XI standards for appraisals. The final rule increases the number of commercial real estate transactions that would require an evaluation by raising the appraisal threshold from \$250,000 to \$500,000. 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 \$31.8 billion in new commercial real estate transactions each year. Assuming that 2.36 to 6.05 percent of

⁷¹ FDIC Call Report, September 30, 2017.

annual originations represent loans with an origination amount greater than \$250,000 but not more than \$500,000, the FDIC estimates that the proposed rule will affect approximately 2,003 to 5,138 loans per year,⁷² or 0.68 to 1.74 loans on average for small FDIC-supervised institutions. Therefore, based on an estimated hourly rate, the final rule would reduce loan review costs for small entities by \$67,391 to \$172,868, on average, each year.⁷³ 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 \$500,000 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 or an appraisal is estimated to be the same at about five minutes for either an appraisal or evaluation.

The final 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 final rule will affect approximately 2,003

⁷² Multiplying \$31.8 billion by 2.36 percent then dividing the product by an average loan amount of \$375,000 equals 2,003 loans and multiplying \$31.8 billion by 6.05 percent then dividing the product by an average loan amount of \$375,000 equals 5,138 loans.

⁷³ The FDIC estimates that the average hourly compensation for a loan officer is \$67.29 an hour. The hourly compensation estimate is based on published compensation rates for Credit Counselors and Loan Officers (\$43.40). The estimate includes the September 2017 75th percentile hourly wage rate reported by the Bureau of Labor Statistics, National Industry-Specific Occupational Employment and Wage Estimates for the Depository Credit Intermediation sector. The reported hourly wage rate is grossed up by 155.0 percent to account for non-monetary compensation as reported by the 3rd Quarter 2017 Employer Costs for Employee Compensation Data. Based on this estimate, loan review costs would decline between \$67,391 (2,003 loans multiplied by 30 minutes and multiplied by \$67.29 per hour) and \$172,868 (5,138 loans multiplied by 30 minutes and multiplied by \$67.29 per hour).

to 5,138 transactions per year,⁷⁴ or 0.68 to 1.74 loans on average for small FDIC-supervised institutions. Therefore, the final rule could reduce loan origination costs for borrowers doing business with small entities by \$2.0 to \$5.1 million on average per year.⁷⁵

By lowering valuation costs on commercial real estate transactions greater than \$250,000 but less than or equal to \$500,000 for small FDIC-supervised institutions, the final 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 final 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 \$500,000.

C. Paperwork Reduction Act

Certain provisions of the final rule contain “collection of information” requirements within the meaning of the Paperwork Reduction Act (PRA) of 1995.⁷⁶ 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 will be extended, without revision. The agencies have concluded that the final rule does not contain any changes to the current information collections; however, the agencies are revising the methodology for calculating the burden estimates. There were no comments received regarding the PRA.

⁷⁴ Multiplying \$31.8 billion by 2.36 percent then dividing the product by an average loan amount of \$375,000 equals 2,003 loans and multiplying \$31.8 billion by 6.05 percent then dividing the product by an average loan amount of \$375,000 equals 5,138 loans.

⁷⁵ Multiplying 2,003 loans by \$1,000 savings equals \$2.0 million and multiplying 5,138 loans by \$1,000 savings equals \$5.1 million.

⁷⁶ 44 U.S.C. 3501-3521.

The OCC and the FDIC submitted the information collection requirements to OMB in connection with the proposal under section 3507(d) of the PRA⁷⁷ and section 1320.11 of the OMB's implementing regulations.⁷⁸ OMB filed a comment pursuant to 5 CFR 1320.11(c) instructing the agencies to examine public comment in response to the proposal and describe in the supporting statement of its next collection (the final rule) any public comments received regarding the collection as well as why (or why it did not) incorporate the commenter's recommendation and include the draft final rule in its next submission. The OCC and the FDIC have resubmitted the collection to OMB in connection with the final rule. The Board reviewed the final rule under the authority delegated to the Board by OMB.

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.

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 institutions⁷⁹ 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

⁷⁷ 44 U.S.C. 3507(d).

⁷⁸ 5 CFR 1320.

⁷⁹ National banks, federal savings associations, SMBs and nonbank subsidiaries of BHCs, insured state nonmember banks and state savings associations, and insured state branches of foreign banks.

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 final rule, regulated institutions will still be required to obtain an evaluation to justify the transaction amount. The agencies estimate that the recordkeeping burden associated with evaluations is the same as the recordkeeping burden associated with appraisals for such transactions.

Current Action: The threshold change in the final 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 final rule will not change the amount of time that institutions 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: 1,200.

Annual Frequency: 1,488.

Total Estimated Annual Burden: 148,800 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: 3,675.

Annual Frequency: 143.

Total Estimated Annual Burden: 43,794 hours.

These collections are available to the public at www.reginfo.gov.

The agencies have an ongoing interest in public comments on its burden estimates. Comments on the collection of information should be sent to:

OCC: Because paper mail in the Washington, DC area and at the OCC is subject to delay, commenters are encouraged to submit comments by e-mail, if possible. Comments may be sent to: Legislative and Regulatory Activities Division, Office of the Comptroller of the Currency, Attention: 1557-0190, 400 7th Street, SW., Suite 3E-218, Mail Stop 9W-11, Washington, DC 20219. In addition, comments may be sent by fax to (571) 465-4326 or by electronic mail to regs.comments@occ.treas.gov. You may personally inspect and photocopy comments at the OCC, 400 7th Street, SW., Washington, DC 20219. For security reasons, the OCC requires that visitors make an appointment to inspect comments. You may do so by calling (202) 649-6700. Upon arrival, visitors will be required to present valid government-issued photo identification and submit to security screening in order to inspect and photocopy comments.

All comments received, including attachments and other supporting materials, are part of the public record and subject to public disclosure. Do not include any information in your comment or supporting materials that you consider confidential or inappropriate for public disclosure.

Board: Nuha Elmaghrabi, Federal Reserve Clearance Officer, Office of the Chief Data Officer, Mail Stop K1-148, Board of Governors of the Federal Reserve System, Washington, DC 20551, with copies of such comments sent to the Office of Management and Budget, Paperwork Reduction Project (7100-0250), Washington, DC 20503.

FDIC: You may submit comments, which should refer to “Real Estate Appraisals, 3064-0103” by any of the following methods:

- Agency Web Site: <http://www.fdic.gov/regulations/laws/federal/>. Follow the instructions for submitting comments on the FDIC Web site.
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- Email: comments@FDIC.gov. Include “Real Estate Appraisals, 3064-0103” in the subject line of the message.

- Mail: Jennifer Jones, Attn: Comments, Federal Deposit Insurance Corporation, 550 17th Street, N.W., MB-3105, Washington, DC 20429.
- Hand Delivery: Comments may be hand delivered to the guard station at the rear of the 550 17th Street Building (located on F Street) on business days between 7 a.m. and 5 p.m.

Public Inspection: All comments received will be posted without change to <http://www.fdic.gov/regulations/laws/federal/> including any personal information provided.

Additionally, commenters may send a copy of their comments to the OMB desk officer for the PRA Agencies by mail to the Office of Information and Regulatory Affairs, U.S. Office of Management and Budget, New Executive Office Building, Room 10235, 725 17th Street, NW., Washington, DC 20503; by fax to (202) 395-6974; or by email to oir_submission@omb.eop.gov.

D. 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.⁸⁰ 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.⁸¹

The final rule reduces burden and does 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 \$500,000), lenders are required to get an evaluation if they chose not to get

⁸⁰ 12 U.S.C. 4802(a).

⁸¹ 12 U.S.C. 4802(b).

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 \$500,000, IDIs can continue to get appraisals instead of evaluations. Because the final rule imposes 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, the agencies are making 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 and finalizing the rule. In designing the scope of the threshold increase, the agencies chose to largely 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 threshold at a level designed to provide significant burden relief without sacrificing safety and soundness. In the proposal, the agencies invited comments on compliance with the Riegle Act, but no such comments were received.

E. Solicitation of Comments on Use of Plain Language

Section 722 of the Gramm-Leach-Bliley Act⁸² requires the agencies to use plain language in all proposed and final rules published after January 1, 2000. The agencies invited comment on how to make the rule easier to understand, but no such comments were received.

F. OCC Unfunded Mandates Reform Act of 1995 Determination

The OCC has analyzed the final rule under the factors in the Unfunded Mandates Reform Act of 1995 (UMRA) (2 U.S.C. 1532). Under this analysis, the OCC considered

⁸² Pub. L. 106-102, section 722, 113 Stat. 1338 1471 (1999).

whether the final 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 final rule does not impose new requirements or include new mandates. Therefore, we conclude that the final 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

12 CFR Part 323

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 amends 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 single 1-to-4 family residential property.

* * * * *

- 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 \$500,000 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 \$500,000.* All federally related transactions that are commercial real estate transactions having a transaction value of more than \$500,000 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:

§ 225.62 Definitions.

* * * * *

(e) *Commercial real estate transaction* means a real estate-related financial transaction that is not secured by a single 1-to-4 family residential property.

* * * * *

3. 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 \$500,000 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 \$500,000.* All federally related transactions that are commercial real estate transactions having a transaction value of more than \$500,000 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:

§ 323.2 Definitions.

* * * * *

(e) *Commercial real estate transaction* means a real estate-related financial transaction that is not secured by a single 1-to-4 family residential property.

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 \$500,000 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 \$500,000.* All federally related transactions that are commercial real estate transactions having a transaction value of more than \$500,000 shall require an appraisal prepared by a State certified appraiser.

* * * * *

[THIS SIGNATURE PAGE RELATES TO THE DOCUMENT TITLED “REAL ESTATE APPRAISALS: FINAL RULEMAKING”]

Real Estate Appraisals: Notice of Final Rulemaking

Dated: [].

[Joseph M. Otting]

Comptroller of the Currency

[THIS SIGNATURE PAGE RELATES TO THE DOCUMENT TITLED “REAL ESTATE APPRAISALS: NOTICE OF FINAL RULEMAKING”]

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

[Margaret McCloskey Shanks,]

Deputy Secretary of the Board.

Real Estate Appraisals: Notice of Final Rulemaking

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

By order of the Board of Directors.

Federal Deposit Insurance Corporation.

[Robert E. Feldman,]

Executive Secretary.