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Proposed Appraisal Requirements Would Exempt More Transactions

January 31, 2019 | Joseph ("Jed") E. Mayk

The Office of the Comptroller of the Currency, Federal Reserve, and Federal Deposit Insurance Corporation (the "Regulators") recently issued a notice of proposed rulemaking that seeks to amend exemptions to appraisal requirements for certain regulated depository institutions. Currently, an exemption applies to real estate transactions of $250,000 or less, and the amendment would raise that threshold to $400,000 or less. Additionally, the recently enacted Economic Growth, Regulatory Relief and Consumer Protection Act (the "Act") exempts from the appraisal requirement certain residential transactions in rural areas (the "Rural Exemption"). The amended regulations would also incorporate this change, however, if the Regulators retain the $400,000 threshold in the final rule, the Rural Exemption will be superfluous.

Background

Under Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, certain regulated depository institutions must obtain appraisals for real estate transactions. These appraisals must be:

- Performed in accordance with uniform standards of professional appraisal practice;
- In writing; and
- Subject to review for compliance with the uniform standards.

The appraisal requirement is intended both to ensure the safety and soundness of regulated institutions by accurately valuing their real estate security and to provide consumer protection by facilitating the informed use of credit. Appraisals generally cost between $375 and $900, with that cost usually passed on to the consumer. The proposed amendments seek to reduce the time and cost burden associated with appraisals, while ensuring the safety and soundness of regulated institutions.

Importantly, however, the appraisal regulations do not affect applicable appraisal requirements for loans insured/guaranteed by the Federal Housing Administration and the Department of Veterans affairs or loans that are sold to Fannie Mae or Freddie Mac.

Nonetheless, the effect on the remaining transactions would be significant. The

Regulators estimate that in 2017 approximately 91% of all mortgages originated in the United Sates were not subject to the depository institution appraisal regulations because they either were not originated by a regulated institution, were sold to GSEs, were insured or guaranteed by a U.S. agency, or were under the $250,000 threshold. The current $250,000 threshold exempted 56% of the transactions, resulting in 750,000 exempt transactions. It is estimated that the new exemptions will cover an additional 16% of all transactions, or roughly 214,000 transactions. Although this results in 72% of transactions being exempted, the total dollar amount of the exempted transactions would remain relatively small in comparison to the total market. The 28% of transactions which are not exempt represent 65% of the total dollar volume of sales.

Exemptions

Current regulations include several significant exemptions from the appraisal requirements, including:

- Residential real estate transactions under $250,000;
- Certain commercial real estate transactions under $500,000 and qualifying business loans of $1,000,000 or less;
- Certain loans insured or guaranteed by, or eligible for sale to, a federal agency or government-sponsored agency;
- Loans for which the appraisal conforms to applicable Fannie or Freddie requirements.

The residential real estate exemption amount has not been changed since 1994. The proposed regulation would increase the residential real estate transaction exemption to $400,000.

Additionally, the Act exempted certain rural transactions from the appraisal requirement. Under the Act, this Rural Exemption applies if:

- The property is located in a rural area;
- The lender provides certain disclosures to the consumer within 3 days of providing the closing disclosure about attempts to contact certified appraisers;
- The transaction value is less than $400,000; and
- The mortgage originator is subject to oversight by a Regulator.

Additionally, an originator making a loan without an appraisal under the Rural exemption is prohibited from selling the loan unless it met certain requirements.

Because the Rural Exemption only applies if the transaction value is less than $400,000, the proposed exemption for transactions of $400,000 or less will cover all transactions under the Rural Exemption.

Use of Evaluations

For some exempt transactions-including those covered by the $400,000 threshold exemption-however, financial institutions must still evaluate the transaction in a manner consistent with safe and sound banking practices. These evaluations should contain sufficient information and analysis to support the institution's decision, but they do not need to meet the uniform standards of professional appraisal practice. Additionally, evaluations can more easily be performed in-house by smaller financial institutions, further reducing costs. The Regulators also seek comments on several questions related to the value of evaluations for consumers and the use of publicly available information in consumer real estate transactions.

Invitation for Comments

As part of the proposed rulemaking, the Regulators seek comments on a number of questions, including:

- What information would consumers lose from the use of evaluations instead of appraisals?
- What benefits do appraisals or evaluations give consumers, and how do those benefits change?
- How useful are publicly available sources about property valuation for consumers?
- How are evaluations created internally or by third parties, and do financial institutions impose requirements to ensure independent analysis?
- Is the $400,000 cutoff appropriate?
- Are there additional consumer protection concerns raised by the proposal?

The Regulators also asked for additional data related to their estimates of the regulatory burden imposed by the existing appraisal requirements.

Comments must be submitted by February 5, 2019.

Hudson Cook, LLP is a national law firm representing the financial services industry in compliance, privacy, litigation, regulatory and enforcement matters.

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