12/2/2018

Gerard S. Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314–3428

RE: Comments on Proposed Rule part 722, Real Estate Appraisals

Secretary Poliquin:

The undersigned professional appraisal organizations appreciate the opportunity to provide our views in regard to the above captioned rulemaking. We strongly believe that a comprehensive, objective understanding of collateral values is essential to the broader real estate finance industry. As such we have significant concerns with the NCUA's proposed rule as it relates to a reduction in reliance on professional appraisers in favor of non-appraisal value opinions.

We believe there should be no change to the residential real estate appraisal threshold.

As part of its proposal, NCUA solicits comment on "factors that should be considered in evaluating the current threshold for 1-to-4 family residential transactions and whether the threshold can and should be raised". We oppose any change to the current 1-to-4 family residential threshold and believe that the rationale for its maintenance as part of the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA) review conducted by the other Federal banking agencies is persuasive.

The rationale, as expressed in the proposal, is tripartite: One, that such an increase would do little if any to alleviate burdens on regulated entities since appraisals would still be required by government guarantors, insurers, or sponsored enterprises; Two, that appraisals provide an essential consumer protection that was further codified into FIRREA as part of the Dodd-Frank Wall Street Reform Act of 2010; and Three, that the 2008 financial crisis exposed the fact that "imprudent mortgage lending can pose significant risks to financial institutions".[1]

None of the underlying facts have changed significantly since the conclusion of the EGRPRA review, and as such remain compelling reasons for continuing to align the NCUA's 1-to-4 family residential threshold with that of the other Federal banking agencies.[2] Moreover, the NCUA's efforts to better clarify how "complex" transactions are quantified and handled as part of this proposal can help affected credit unions better understand when they can solicit the services of a state licensed appraiser, and ways in which to handle the discovery that an assignment is "complex" without necessarily requiring a second full appraisal by a state certified appraiser.

---

[1] See Proposed Rule at 49858.

[2] The undersigned are aware of the proposal recently announced by the Federal Reserve, Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency that would raise the existing $250,000 threshold to $400,000. Our position is that, globally, the threshold for all agencies should remain at $250,000.

Such clarity should ease the burden for obtaining an appraisal on non-exempt 1-to-4 family residential transactions, and buttresses existing arguments for not changing the threshold.

The NCUA's reasoning for a simplified $1 million threshold for all non-residential lending is not supported by the very statements contained in the proposal, and should not be changed.

As NCUA itself acknowledges in the proposal:

> Analysis of supervisory information concerning losses on commercial real estate transactions suggests that faulty valuations of the underlying real estate collateral have not been a material cause of losses. In 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 and credit union failures. Supervisory experience and a review of material loss reviews covering those decades suggest that factors other than faulty appraisals were the cause(s) for an institution's loss experience. [Footnotes omitted.][3]

Simply restated, the current valuation requirements for non-residential transactions have been the strength of the overall lending system and provide a critical backstop for faults in the underwriting and administration functions of a loan. This dynamic not only countermands the proposal's efforts to dilute valuation requirements but could be used to argue for *stronger* valuation requirements to compensate for weakness in the other legs of the lending stool.

The growth in exempted transactions is unreasonable on its face, and the data used to determine the impacted universe or transactions is acknowledged as faulty.

As cited in the proposal, the number of transactions exempted under an increase in the threshold to $1 million for both QBL and non-QBL loans would go "from 27 percent to 66 percent if the threshold were raised from $250,000 to $1 million"; restated, it would shift from one in four transactions being exempted, to two in three becoming exempt. On a dollar value basis, NCUA anticipates the amount to "increase from 1.8 percent to 13 percent".[4] While 13 percent may seem inconsequential, it represents more than seven times increase in the total dollar value now being exempt from appraisal requirements.

However it is stated, this marks a sharp increase in the total volume of activity that would now be exempt from appraisal requirements. While NCUA urges that "incremental risk can be controlled through sound risk management practices"[5], it goes on to criticize risk management practices as a leading cause of nonperformance in the very next column. Such internal inconsistency calls into question the basis of the proposal as a whole.

Additionally, NCUA acknowledges in Footnote 68 that the dataset used to determine the universe of transactions that would now be exempt from appraisal requirements (the CoStar Comps database) has issues with the exact kind of "sales of smaller properties and transactions in

---

[3] See Proposed Rule at 49866.
[4] See Proposed Rule at 49865-6.
[5] See Proposed Rule ay 49866.

rural markets" that are very likely to be exempt under the proposed changes. Because of this, the total impact is likely understated by NCUA and could be magnitudes larger than already established in the proposal.

The proposal deviates from other Federal banking agencies in establishing a single, higher dollar threshold for all non-residential transactions.

Through the EGRPRA process, the other Federal banking agencies reviewed questions surrounding the appropriateness of having two different thresholds for non-residential appraisal requirements depending on whether the loan was part of a purchase transaction where the property was being collateralized, or if the collateral was security against a general qualified business loan. In deciding to ultimately raise the non-QBL threshold to $500,000, the other agencies implicitly stated that having two discreet thresholds based on the nature of the commercial loan being originated made sense from a safety and soundness perspective, as each type of loan presents distinct risks that must be considered during underwriting.[6]

NCUA, in shaping its argument for a single, higher threshold at $1 million, relies on the statutory ceiling of 1.75 times a credit union's net worth for total volume of commercial loans of all types as a limiting factor that controls for safety and soundness in a way that does not exist at other lending institutions that do not have such a limitation.[7] While the total volume of assets tied into commercial lending is smaller in credit unions than in other lending institutions, the statutory ceiling indicates an awareness of the unique risks and challenges with lending in the commercial space, and more so when distinguishing between a commercial real estate purchase and business loans collateralized by existing commercial real estate assets. These risks do not change based on the institution originating the loan, and therefore should be considered in the same way as the other Federal banking agencies and handled using a two-threshold solution like the other agencies.

The non-appraisal written estimates of market values, though guided by the Interagency Appraisal and Evaluation Guidelines, are not as robust as a USPAP-compliant appraisal or evaluation.

To the extent that collateral valuations are still required for those transactions that would be exempt from appraisals under the proposal, these written estimates of market values reflect a significant reduction both in quality and reliability from an opinion developed under the Uniform Standards for Professional Appraisal Practice, or USPAP. Not only does USPAP create enforceable standards that practitioners must follow, it can be used both in an appraisal and an evaluation context. While the Interagency Appraisal and Evaluation Guidelines (IAEG) provide some expectation for what the credit union can reasonably rely on for a collateral value when originating the loan, the IAEG requirements fall far short of what would be expected under a USPAP standard. At a minimum, we would encourage NCUA and its regulated credit unions to adhere to USPAP as frequently as possible, even in an evaluation assignment or those situations contemplated in rural areas.

---

[6] See Proposed Rule at 49859.
[7] See Proposed Rule at 49865.

One additional concern to raise here deals with the independence – or lack thereof – of the individual who may be tasked with completing a written estimate of market value. While appraisers are bound by USPAP to remain objective and have no interest whatsoever in the underlying transaction, the safeguards contemplated in the proposal seem somewhat malleable where an individual cannot be fully outside of the loan production and collection process. While we expect many credit unions to impose the prudent safeguards asked by NCUA, the lack of specificity as to what the safeguards might look like and the potential for abuse of these kinds of arrangements are cause for concern, and underscore why reliance on an independent appraiser for any value conclusion is still the safest course of action for credit unions.

Finally, using the cost of comparable valuation products as a justification for relying on written estimates of market value is short-sighted at best.

The proposal's discussion on the subject of costs for valuation products is as follows:

> [T]he 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. Nonresidential real estate transactions with values above $250,000, but below $1 million (applicable transaction value range), are likely to involve smaller and less complex properties, and appraisals and evaluations on such properties would likely be at the lower end of the cost range. **This third-party pricing information suggests a savings of several hundred dollars per transaction.** [Emphasis added.][8]

Using the low-end numbers provided by NCUA, the expected cost savings provided by the shift to written estimates of market value from appraisals is $500 per transaction. However, the cost differential does not account for either the difference in quality between the two valuation options, nor does it factor in the ability to seek enforcement action against an appraiser who is believed to have not complied with USPAP or other relevant state laws (where no such enforcement mechanism would exist for the individual providing the written estimate).

The idea here of saving hundreds of dollars now, versus the potential exposure to losses of hundreds of thousands of dollars later, seems to forget any of the key lessons from the 2008 economic downturn. That the dollar cost should outweigh any potential benefits from an appraisal either ignores the differences between the two options presented or chooses not to acknowledge any difference in the first place.

We are concerned that the underlying reasons for relying on the 1994 regulations – the robustness of agency and enterprise appraisal requirements – are being eroded.

One specific statement, in discussing the 1994 interagency regulations, gives us concerns about whether and to what extent NCUA assessed current valuation trends in crafting the proposal:

> When the other banking agencies (and subsequently the NCUA) adopted current § 722.3(a)(7) in 1994, it was based on the presumption that any U.S. government agency's or sponsored agency's insurance or guarantee program would have a prudent appraisal requirement. **The NCUA continues to believe this to be the case**. [Emphasis added.]

[8] See Proposed Rule at 49864-5.

As the NCUA is likely aware, both Fannie Mae and Freddie Mac have moved in recent months to waive appraisal requirements entirely for both purchase money mortgage transactions and refinance transaction. These GSEs are also actively evaluating the usability of so-called "hybrid" appraisals where the field inspection of the subject property is completed by a third party unrelated to the appraiser who, in turn, completes what amounts to a desktop appraisal using the third-party information; the same solution has also been proposed for the VA through House legislation[9]. There is also movement to rely more on "big data" automated valuation solutions, and even platforms that utilize borrower-provided interior photographs to help populate the valuation report.

To categorically state that all agencies and sponsored enterprises are still deploying "prudent" appraisal requirements either shows unfailing confidence in these new and emerging valuation products, or a lack of awareness of the shifting valuation landscape and the yet unknown risks it poses. We would encourage NCUA to drill down further in these areas to ensure continued comfort with other entities' appraisal requirements. We also question whether and to what extent reliance on such emerging valuation products comports with NCUA's – and other agencies – core responsibilities that arise from Title XI.

We appreciate having the opportunity to share our views. If you wish to discuss our views further, please contact John D. Russell, JD, Senior Director of Government Relations and Business Development for the American Society of Appraisers at 703-733-2103, or by email at jrussell@appraisers.org, or Stephen Frerichs, Government Relations Consultant for the American Society of Farm Managers and Rural Appraisers at 703-212-9416, or by email at sfrerichs8@comcast.net.

Sincerely,
American Society of Appraisers
American Society of Farm Managers and Rural Appraisers
California Coalition of Appraisal Professionals
Delaware Association of Appraisers, Inc.
Maryland Association of Appraisers
Michigan Coalition of Appraisal Professionals
Mississippi Coalition of Appraisers
North Carolina Real Estate Appraiser Association
South Carolina Professional Appraisers Coalition
Tennessee Appraiser Coalition

[9] See HR 299, 115th Congress, entitled Blue Water Vietnam Veterans Act of 2017, Section 7.