April 9, 2020

Memorandum to: The Board of Directors

From: Doreen R. Eberley
Director
Division of Risk Management and Supervision

Nicholas J. Podsiadly
General Counsel
Legal Division

Subject: Interim Final Rule on Temporary Deferral of Real Estate Appraisals and Evaluations

Recommendation

Staff recommends that the Board of Directors (Board) of the Federal Deposit Insurance Corporation (FDIC) adopt and issue the attached Interim Final Rule (IFR) titled Real Estate Appraisals: Interim Final Rule (12 CFR Part 323). The FDIC would issue the IFR jointly with the Office of Comptroller of the Currency and the Board of Governors of the Federal Reserve System (collectively referred to as the Agencies). The IFR amends the rule entitled Real Estate Appraisals set forth in title 12, part 323 of the Code of Federal Regulations (12 CFR Part 323),[1] to create a new exception to general appraisal requirements that would temporarily defer the requirement to obtain an appraisal or evaluation for up to 120 days following the closing of a transaction for certain residential and commercial real estate transactions.

This relief is being provided to allow insured depository institutions to expeditiously extend liquidity to creditworthy households and businesses in light of recent strains on the U.S. economy as a result of the coronavirus disease 2019 (COVID-19). A regulated institution would still be expected to make best efforts to obtain a reliable valuation of real property collateral before a loan closing, consistent with the principles in the Agencies' Standards for Safety and Soundness[2] and Real Estate Lending Standards.[3]

The IFR would become effective immediately upon publication in the *Federal Register*. Comments on the IFR would still be solicited, however, for a period of 45 days from the date of publication in the *Federal Register*. The new exception to general appraisal requirements would expire on December 31, 2020.

[1] FDIC: 12CFR Part 323.
[2] FDIC: 12 CFR Part 364, Appendix A.
[3] FDIC: 12 CFR Part 365, Appendix A to Subpart A.

Background

Impact of COVID-19 on appraisals and evaluations

Due to the impact of COVID-19, businesses and individuals have a heightened need for additional liquidity. Being able to quickly access equity in real estate could help address this need. However, government restrictions on non-essential movement and health and safety advisories in response to COVID-19, including those relating to social distancing have caused complications with respect to performing and completing real property appraisals and evaluations needed to comply with federal appraisal regulations. As a result, some borrowers may experience delays in obtaining funds needed to meet immediate and near-term financial needs.

Title XI and the appraisal regulations

Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act[4] (FIRREA) directs each Federal financial institutions regulatory agency to publish appraisal regulations for federally related transactions within its jurisdiction. The purpose of Title XI is to protect federal financial and public policy interests in real estate-related transactions by requiring that real estate appraisals used in connection with federally related transactions (Title XI appraisals) are performed in writing, in accordance with uniform standards, by individuals whose competency has been demonstrated and whose professional conduct will be subject to effective supervision.

Title XI directs the Agencies to prescribe appropriate standards for Title XI appraisals under the Agencies' respective jurisdictions. At a minimum, the statute provides that a Title XI appraisal must be: (1) performed in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP); (2) a written appraisal, as defined by the statute; and (3) subject to appropriate review for compliance with USPAP. Although appraisals are ordinarily completed before a lender and borrower close a real estate transaction, there is no specific requirement in USPAP that appraisals be completed at a specific time relative to the closing of a transaction.

All federally related transactions must have Title XI appraisals. Title XI defines a federally related transaction as a real estate-related financial transaction, which the Agencies or a financial institution regulated by the Agencies engages in or contracts for, that requires the services of an appraiser. The Agencies have authority to determine which real estate-related financial transactions do not require the services of an appraiser and thus are not required to have Title XI appraisals. The Agencies have exercised this authority by exempting certain categories of real estate-related financial transactions from the Agencies' appraisal requirements.

The Agencies have used their safety and soundness authority to require evaluations for a subset of transactions for which an appraisal is not required. Under the appraisal regulations, for these transactions, financial institutions that are subject to the Agencies' appraisal regulations (regulated institutions) must obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.

[4] See at https://www.fdic.gov/regulations/laws/rules/8000-3100.html.

The Interim Final Rule

Authority to defer appraisals and evaluations

Under the IFR, deferrals of appraisals and evaluations will allow for expeditious access to credit and will be temporary. The deferrals are offered in response to a national emergency and incorporate the principles in the Agencies' Standards for Safety and Soundness and Real Estate Lending Standards that focus on the ability of a borrower to repay a loan and other relevant factors. These deferrals would not be an exercise of the Agencies' waiver authority, because appraisals and evaluations are being deferred, not waived. The deferrals also would not be a waiver of USPAP requirements, given that: (1) USPAP does not address or correlate the completion of an appraisal assignment with the timing of a lending decision; and (2) when the deferred appraisal is conducted it must be done in compliance with USPAP.

The deferral of evaluations reflects the same considerations relating to COVID-19. The Agencies require evaluations for certain exempt transactions as a matter of safety and soundness. Evaluations do not need to comply with USPAP, but must be sufficiently robust to support a valuation conclusion. Evaluations can be less complex than an appraisal and usually take less time to complete, but also commonly involve physical property inspections. For these reasons, the Agencies would also use their safety and soundness authority to defer evaluations.

By the end of the deferral period, regulated institutions would be required to obtain appraisals or evaluations that are consistent with safe and sound banking practices as required by the Agencies' appraisal regulations.

Summary of the IFR

The IFR would temporarily defer requirements for appraisals and evaluations for all residential and commercial real estate secured transactions, including loans for new money or refinancing transactions, but excluding loans for acquisition, development and construction. The deferral would not apply to real estate secured loans for the acquisition, development, and construction of commercial or residential property because repayment is generally dependent on the completion or sale of the property being held as collateral as opposed to repayment generated by existing collateral or the borrower's income.

Under the IFR, regulated institutions may close a real estate loan without a contemporaneous appraisal or evaluation, subject to a requirement that institutions obtain the appraisal or evaluation, as would have been required under the appraisal regulations without the deferral, within a grace period of 120 days after closing of the transaction. While appraisals and evaluations can be deferred, the Agencies would continue to expect regulated institutions to adhere to internal underwriting standards for assessing borrowers' creditworthiness and repayment capacity, and to develop procedures for initially estimating the collateral's value upon which to extend or refinance credit.

The agencies also expect institutions to develop an appropriate risk mitigation strategy if the appraisal or evaluation ultimately reveals a market value significantly lower than the expected

market value. In addition, the Agencies would also expect institutions to comply with applicable laws and regulations, including those relating to consumer protection.
The temporary provision permitting regulated institutions to defer an appraisal or evaluation for eligible transactions would expire on December 31, 2020, unless extended by the Agencies.

Revisions to the Title XI Appraisal Regulations

The IFR would add a new, temporary provision to the appraisal regulations that provides a 120-day deferral of appraisal and evaluation requirements for covered transactions secured by commercial or residential real estate during the COVID-19 pandemic. The IFR would define covered transactions as all residential and commercial real estate secured transactions, excluding transactions for acquisition, development, and construction of real estate. The IFR would not revise any of the existing appraisal exceptions or requirements for evaluations.

The scope of covered transactions would allow regulated institutions to quickly provide liquidity to owners of commercial and residential property while mitigating risks to safety and soundness. The limited timeframe for the deferral should in some respects help reduce potential risk by balancing the need for immediate relief due to the national emergency with safety and soundness concerns for risk to lenders.

Conclusion:

Staff recommends the Board approve the publication of the attached IFR titled "Real Estate Appraisals; Interim Final Rule" in the *Federal Register*.

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