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National Association of Federally-Insured Credit Unions

December 3, 2018

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

RE: Real Estate Appraisals (3133-AE79)

Dear Mr. Poliquin:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), the only national trade association focusing exclusively on federal issues affecting the nation's federally-insured credit unions, I am writing to you in regard to the National Credit Union Administration's (NUCA) proposed rule regarding real estate appraisal requirements.

NAFCU generally supports the proposed amendments to the NCUA's appraisal rules, which are required under Title XI of the *Financial Institutions Reform, Recovery, and Enforcement Act of 1989* (Title XI). NAFCU anticipates that the new threshold for required appraisals in commercial real estate transactions will address appraiser capacity issues that have been observed in smaller markets, and which have contributed to unnecessary delays and increased costs for borrowers. In essence, NAFCU believes the proposed rule will improve access to credit by reducing closing times and transaction costs. Furthermore, NAFCU believes the threshold adjustment more appropriately reflects the actual risk of commercial real estate transactions, while still preserving strong safety and soundness standards for credit unions.

General Comments

NAFCU believes that the framework advanced in the proposal, which modestly improves the clarity of the current regulation while meaningfully reducing regulatory burden in connection with commercial real estate transactions, represents the type of deregulatory action that is long overdue for the credit union industry. NAFCU also appreciates the agency's decision to incorporate new language that accounts for Section 103 of the *Economic Growth, Regulatory Relief, and Consumer Protection Act* (S. 2155), which provides appraisal relief for certain federally-related, rural real estate transactions valued below \$400,000 if no state-certified or state-licensed appraiser is available. Although Section 103 is self-implementing, credit unions should benefit from the additional clarification in the regulatory text.

The decision to increase the appraisal threshold for commercial real estate-related transactions is a positive development that aligns credit unions' collective risk profile with evolving regulatory expectations for appraisals. Judging from years of historically sound valuation practices, NAFCU

believes that credit unions are readily capable of exercising prudent judgment in commercial transactions valued below \$1 million when determining whether to use an appraisal or a written estimate of market value. Appraisal practices have not raised safety and soundness concerns that would warrant the current appraisal threshold of \$250,000 for commercial real estate transactions. The supervisory analysis provided in the proposal supports this conclusion. NAFCU agrees with the NCUA that faulty valuations of underlying real estate collateral have not been a material cause of losses, and that the primary underwriting factor in commercial transactions is the cash flow of the business. Furthermore, as the NCUA's experience and material loss reviews indicate, faulty appraisals were not the cause of credit unions' loss experience during the financial crisis.

Accordingly, NAFCU supports the NCUA's decision to increase the threshold at which non-residential real estate-related financial transactions are exempt from appraisal requirements from \$250,000 to \$1 million.

Complex Residential Real Estate Transactions

NAFCU supports clarification of the definition for complex residential real estate transactions, which provides that a credit union may presume that appraisals of one-to-four family residential properties are not complex unless the institution has readily available information that a given appraisal will be complex. NAFCU believes that the amended definition better reflects the appraisal rule's existing contents but presents the information more clearly.

NAFCU does not agree with newly proposed appraisal requirements for complex residential real estate transactions that are partially insured or guaranteed by a U.S. government agency or U.S. government sponsored agency, but have \$250,000 or more of the transaction value not insured or guaranteed, and which are not otherwise exempt. The proposed requirement to have a state-certified appraisal for such transactions would contribute to regulatory burden without meaningfully enhancing the safety and soundness of the credit union industry. Furthermore, these transactions are exempt from appraisal requirements under the current rule, and there is no indication that current valuations represent a supervisory concern or pose an undue risk to the Share Insurance Fund. In general, residential appraisals are less complex than commercial appraisals. To the extent that the NCUA seeks to reconsider the existing threshold for complex, residential real estate-related transactions that are only partially insured, NAFCU believes that lowering the threshold is appropriate and can be done without impairment to safety and soundness principles.

Appraisal Threshold for Residential Real Estate Transactions

The proposal solicits comment on whether the NCUA should reconsider the current appraisal threshold for one-to-four family residential transactions and what factors should guide such a decision. NAFCU believes the NCUA should seek to raise the \$250,000 appraisal threshold which currently applies to one-to-four family residential transactions. The treatment of residential real estate loans in the NCUA's risk-based capital rule, when compared with commercial loans, suggests that there is an opportunity to recalibrate appraisal requirements to match risk assumptions. Additionally, greater transparency and technological innovation in the past decade

provide for significantly more detailed information about trends in the residential market, including collateral valuations, which should further alleviate safety and soundness concerns.

NAFCU also believes that the NCUA's conclusion about the limited relief that would follow from an adjustment to the residential appraisal threshold should be reconsidered. While it is true that appraisals would still be required for a large percentage of residential real estate transactions, pursuant to the rules of the federal housing agencies and the standards set by the government-sponsored enterprises (GSEs), there may be opportunities for future relief which the NCUA should not prematurely foreclose. Already there is some evidence that the GSEs are willing to waive appraisal requirements in certain circumstances.

Freddie Mac's Automated Collateral Evaluation tool and Fannie Mae's Property Inspection Waiver programs offer ways for financial institutions to benefit from existing databases of appraisal information and streamline underwriting by providing—in certain circumstances—only a written estimate of market value. NAFCU encourages the NCUA to evaluate these developments to determine whether potential relief from an adjusted residential real estate appraisals threshold may be greater than originally anticipated.

The NCUA should also consider the limited consumer protection benefit derived from an artificially low appraisal threshold for residential real estate transactions. The proposal cites the view of the Bureau of Consumer Financial Protection (Bureau) that appraisals can provide consumer protection benefits and that there may be risks to consumers resulting from an expansion of the number of residential mortgage transactions that would be exempt from the Title XI appraisal requirement. However, the benefit of a lender ordered appraisal is primarily to protect the credit union against the risk of default. Written estimates can adequately serve this function and credit unions have every incentive to exercise sound judgment when determining whether an appraisal is needed to assess the value of real-estate collateral. In the absence of more detailed Bureau analysis or data regarding potential consumer protection issues, the NCUA should explore the possibility of raising the threshold.

A recent proposal jointly issued by the Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and the Board of Governors of the Federal Reserve System ("other banking agencies") should serve as additional evidence that reconsideration of the residential appraisal threshold is appropriate. The proposal would increase the appraisal requirement for residential transactions from \$250,000 to \$400,000, a level that does not pose safety and soundness concerns according to the other banking agencies. NAFCU believes that the NCUA should, at a minimum, consider similar amendments to Part 722 to ensure parity with bank rules for residential real estate transactions.

Real Estate-Related Transactions That Are Fully or Partially Guaranteed by a U.S. Government Agency or U.S. Government Sponsored Agency

The proposal eliminates the current exemption for appraisal and written estimate of market value requirements for real estate-related financial transactions that are fully or partially guaranteed by a U.S. government agency or U.S. government sponsored agency. Under the current rule, this is a categorical exemption that applies regardless of whether the insurance or guarantee is for the full

transaction value or only a part of the transaction value. As noted in the preamble, this exemption was adopted based on the presumption that a U.S. government agency's or sponsored agency's insurance or guarantee program would have an appraisal requirement. While the NCUA anticipates that such a presumption could no longer apply, the other banking agencies chose not to eliminate this exemption from their own appraisal rules, even as the GSEs have started to experiment with more flexible appraisal requirements. Accordingly, NAFCU believes that absent more definitive information regarding the development of guarantee and insurance program appraisal requirements, it would be premature for the NCUA to eliminate the exemption in current § 722.3(a)(7). Furthermore, such a change might impair future efforts to promote flexibility that are perhaps best informed by the experiences of the GSEs.

De Minimis Threshold for Transactions that are Partially Insured or Guaranteed

With respect to written estimate requirements for transactions that are partially insured or guaranteed by an agency or government sponsored agency, NAFCU would support efforts by the NCUA to establish an exemption from the written estimate requirement when the uninsured or unguaranteed portion is below a certain amount. An appropriate de minimis threshold could be \$50,000, as the NCUA suggests. NAFCU believes that credit unions already exercise sound judgment when assessing the risk of underlying collateral. For lower value transactions, the cost of preparing a written estimate may be unnecessary given the credit union's experience and familiarity with the locality involved. Accordingly, NAFCU believes the NCUA should establish a de minimis threshold to encourage flexibility and reduce borrower costs.

Exemption for Existing Extensions of Credit

The proposed rule would amend current §722.3(a)(5) by providing that an existing extension of credit would not require an appraisal or written estimate of market value if the transaction is not considered a new loan under Generally Accepted Accounting Principles (GAAP). As the proposal acknowledges, there may be circumstances where the new definition necessitates an appraisal that would not otherwise be needed under the current rule; however, it is unclear whether this would be a common scenario or whether the GAAP definition is well-suited to valuation practices.

If the NCUA believes that the current definition for an existing extension of credit is unreasonably difficult to apply in practice, then the justification for any new definition should clearly explain the tradeoffs in terms of enhanced objectivity versus impaired flexibility. Furthermore, other components of the regulation that are equally subjective have not warranted significant revision, such as the definition of "complex," which refers generally to atypical conditions.

Given that the other banking agencies chose not to modify the language pertaining to existing extensions of credit in their May 2018 final appraisal rule, NAFCU believes that the NCUA should gather additional data from credit unions before making such a change. Most importantly, the NCUA should ensure that any future change is not more burdensome than the definition adopted by the other banking agencies. NAFCU also encourages the NCUA to codify the policy expressed in the preamble, which states that a written estimate of market value is not required for all modifications, workouts, or troubled debt restructurings of existing loans.

The NCUA's Discretionary Authority to Require Appraisals

NAFCU believes that the NCUA should limit application of its discretionary authority in §722.3(e) if credit unions transition to new appraisal rules. As we have seen in the context of mergers, catchall regulatory language imposes real costs on credit unions that find themselves caught off guard by unannounced agency policies. Furthermore, the use of such discretionary authority—particularly in connection with the more subjective aspects of the appraisal rule—could create industry confusion. If the NCUA is intent on adopting clearer definitions, such as for existing extensions of credit, then it should limit application of its discretionary authority and communicate supervisory expectations unambiguously if there are perceived safety and soundness concerns.

Conclusion

NAFCU appreciates the NCUA's recognition of credit unions' low risk in the proposal, which is reflected in the amended appraisal threshold for commercial real estate-related transactions. The proposed change will improve borrower access to credit while meaningfully reducing regulatory burden. We also encourage the agency to explore increasing the threshold for required appraisals in connection with residential real estate transactions, which would further improve credit unions' ability to close transactions at reduced cost to borrowers. If you have any questions or concerns, please do not hesitate to contact me at (703) 842-2266 or amorris@nafcu.org.

Sincerely,

A handwritten signature in black ink that reads "Andrew Morris". The signature is written in a cursive, flowing style.

Andrew Morris
Senior Counsel for Research and Policy