RESCINDED

Real Estate Appraisal

Replaced by Comptroller's Handbook, Asset Quality series; OCC Bulletin 2018-39; and OCC Bulletin 2010-42

The soundness of real estate loans and investments made by financial institutions depends upon the adequacy of the underwriting standards and credit analysis used to support these transactions. A real estate appraisal or evaluation is one of several essential components of the lending process. For the purpose of collateral administration in a loan portfolio, an institution's estimate of value of real property may be supported by an existing or new appraisal or evaluation.

LINKS
Program
Questionnaire
Appendix A

This Handbook Section provides: (1) examiner guidance on what to look for in a savings association's administration of its appraisal and evaluation programs, (2) guidance as to what should be contained in an appraisal report, (3) guidance on the appropriate evaluation of real estate in those circumstances where an appraisal is not required, and (4) a summary of the OTS appraisal regulation.

Responsibilities of Management and the Board of Directors

The savings association's lending policies are a critical component of a sound underwriting policy. An appraisal or evaluation is an integral part of the decision-making process in credit analysis and investment underwriting. The value of real estate taken as loan collateral provides additional support to the borrower's credit capacity because it can provide a secondary repayment source in the event that the primary repayment source - the borrower's cash flow - fails to permit servicing of the indebtedness in a satisfactory manner. Also, appraisals and evaluations play an important role in administering foreclosed properties, both in the determination of a carrying value and in the establishment of a sale price. For other investments, appraisals and evaluations are used to validate the value of interests in real estate.

The soundness of mortgage loans and real estate investments of both the association and those of its service corporations depends to a great extent upon the adequacy of the loan underwriting. An appraisal standard is one of the most important elements of the underwriting policy because appraisal reports contain estimates of value of collateral held or assets owned. The responsibilities of management include the development, implementation, and maintenance of appraisal standards to determine compliance with the appraisal requirements in Part 564 of the OTS regulations.

The board of directors is responsible for adopting and reviewing policies and procedures that establish effective real estate appraisal and evaluation programs. At a minimum, the programs should:

- incorporate prudent standards and procedures for obtaining initial and subsequent appraisals and evaluations;

- be tailored to the institution's size and location and to the nature of its real estate-related activities;
- establish a method(s) to monitor the value of real estate collateral securing an institution's real estate loans; and
- establish the manner in which an institution selects, evaluates, and monitors individuals who perform or review real estate appraisals and evaluations.

Competency, expertise, independence, and ability to render a high-quality written report are the appropriate selection criteria for appraisers and evaluators.[1]

Savings associations and their subsidiaries are also required to comply with § 564.8, which sets forth the responsibilities of management to develop written appraisal policies to ensure that adequate appraisals are obtained consistent with the requirements of the OTS appraisal rule, to institute procedures pertaining to the hiring of qualified appraisers, and to annually review the performance of appraisers.

Appraisal and Evaluation Compliance Procedures (for all real estate-related transactions)

Institutions should establish procedures to ensure appraisals and evaluations satisfy the technical requirements of Part 564, as well as internal policies and procedures. Checklists may be used to assist an institution's personnel in determining the completeness of appraisals and evaluations. Loan files should contain documentation that the appraisal or evaluation received an appropriate technical compliance check. The technical compliance procedures should provide an assessment to detect deficiencies in appraisals and evaluations. If there are deficiencies that render an appraisal's or evaluation's estimate of value unreliable, the institution should obtain a replacement prior to making its final credit decision. Deficiencies that do not affect the estimate of value should be corrected by the individual who conducted the appraisal or evaluation before the transaction is completed.

Audit/Critique Procedures (for a sample of real estate-related transactions)

Management should also test the substance of appraisals and evaluations through audit procedures. An institution's audit procedures should provide for a critique of selected appraisals and evaluations. The criteria to identify transactions subject to this substance critique should be consistent with prudent audit

[1] To avoid potential conflicts of interest, staff appraisers should not be supervised by loan underwriters, loan officers or collection officers. The OTS recognizes that, in certain cases, it may be necessary for loan officers or other institution-related individuals to perform appraisals or evaluations. Such cases would depend on the institution's particular circumstances. An example would be a small rural institution where the only qualified individual to perform appraisals or evaluation is a loan officer, and separating this person from the loan and collection departments would be difficult. In these situations, the OTS recommends that this individual perform appraisal or evaluation work on loans in which he or she is not otherwise involved. In cases where loan officers or other related individuals perform appraisals, regulated institutions must ensure that the appraisers are licensed or certified and that the appraisals are adequate. Directors and officers should abstain from any vote and/or approval that involves assets on which they have performed an appraisal or evaluation. Sufficient safeguards must be in place to permit appraisers and evaluators to exercise independent judgment.

sampling or testing practices and have a bias toward large credit exposures and loans secured by out-of-area properties and specialized types of properties.

The critique should assess the adequacy, reasonableness, and appropriateness of the methods, assumptions and techniques that were used to perform the appraisal or evaluation. An individual who performs critiques, whether an institution employee or an outside auditor or consultant, should have real estate-related training or experience and be independent of the transaction.

The estimate of value in an appraisal or evaluation may not be changed as a result of a critique. Changes to an appraisal's estimate of value are permitted only as a result of a review conducted in compliance with Standard III of the Uniform Standards of Professional Appraisal Practices (USPAP).

Appraisal and Evaluation Review Procedures (for certain real estate-related transactions)

An institution should have appraisal and evaluation review procedures that are separate from the appraisal and evaluation compliance and audit procedures. An institution should establish criteria consistent with prudent practices that designate those real estate-related transactions whose appraisal or evaluation should be reviewed prior to an institution's decision to extend credit or other decision. Moreover, the frequency and scope of appraisal and evaluation reviews should be established by the board of directors as part of the written policy. For example, an institution may determine appraisals and evaluations on all major loans should be reviewed prior to the decision to extend credit.

If an institution needs to perform a review of an appraisal or evaluation, it may incorporate the above-discussed compliance procedures into the review. An individual conducting an appraisal or evaluation review must have appraisal-related training or experience, but need not be state-licensed or state-certified, except as noted below.

An appraisal or evaluation review will determine the adequacy and relevance of the data in the appraisal or evaluation. The reviewer will assess the reasonableness of analysis, opinions, and conclusions in the appraisal or evaluation. The reviewer will also form an opinion as to the appropriateness of the methods and techniques used in the appraisal or evaluation. The reviewer should determine the propriety of any minor adjustments to the data that do not affect the estimate of value of the real property. The reviewer, however, may not change the value of an appraisal or evaluation through the review process. Appraisal and evaluation reviews should be appropriately documented in the file. If the original appraisal or evaluation is deemed unreliable, a new appraisal or evaluation should be conducted. (If changes in the appraisal are required for the institution's purposes, they can be done by an in-house review appraiser who, for federally related transactions, must be licensed or certified and follow Standard 3 of USPAP.)

Appraisal Management

The association's appraisal policies must ensure that federally related transactions are performed by state-certified or state-licensed appraisers, as appropriate and consistent with § 564.3. Appraisals should reflect professional competence and facilitate the reporting of estimates of market value. Appraisal policies should contain the minimum standards specified under Appraisal Content, comport with safety and soundness, and should be related to the association's lending policies.

Management must develop and adopt guidelines and implement procedures relative to the hiring of appraisers to perform appraisals for the savings association. The guidelines must address, at a minimum, appraiser experience and education requirements that are consistent with the requirements of Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). FIRREA requires that an appraiser's experience and education requirements must, at a minimum, meet those detailed by the Appraisal Standards Board and the Appraiser Qualifications Board of the Appraisal Foundation. The guidelines should also specify that selection of appraisers based on their membership in a specific appraisal organization, or lack thereof, is a prohibited practice.

It is vital that management furnish the appraiser with all information it has available to contribute to the valuation process. Management should furnish the appraiser with an engagement letter and any necessary attachments that may include, but are not limited to, the following information:

- a copy of the savings association's written appraisal policies,
- a copy of the appraisal rule (if not fully included within the savings association's appraisal policies),
- a legal description of the subject property,
- the interest to be appraised,
- the types of value estimates requested,
- financing information,
- income statements of the subject property,
- leases, and
- purchase agreements.

Master engagement letters are acceptable provided the letters contribute to sound underwriting and clarify that the institution does not discriminate against any appraiser based on membership, or lack thereof, in a specific appraisal organization.

Management should review annually the performance of all approved appraisers used within the preceding year to determine compliance with the association's appraisal policies and procedures and the reasonableness of the value estimates reported.

Staff Appraisers

An institution may choose to have its appraisals prepared by a staff appraiser. Such appraisers, however, must be independent of the lending, investment, and collection functions of the institution and have no direct or indirect interest, financial or otherwise, in the properties they appraise. If the only qualified persons available to perform an appraisal are involved in the lending, investment, or collection functions of the institution, appropriate steps must be taken to ensure that the appraisers exercise independent judgment and that the appraisal is adequate. Such steps include prohibiting an individual from performing an appraisal in connection with federally related transactions where the appraiser is otherwise involved and prohibiting directors and officers from participation in any vote or approval that involves assets on which they performed an appraisal.

Fee Appraisers

The savings association, or its agent, must directly engage the appraiser. The appraiser must have no direct or indirect interest, financial or otherwise, in the property or transaction. The savings association may accept an appraisal that was prepared by an appraiser engaged directly by another institution subject to Title XI of FIRREA if: (1) the institution that accepts the appraisal has established procedures for review of real estate appraisals and (2) the institution reviewed the appraisal under its established review procedures, found it acceptable, and documented the review in writing.

Appraisals Required

A state-certified appraiser must prepare an appraisal in the following circumstances:

- All federally related transactions having a transaction value of $1,000,000 or more.
- All nonresidential transactions with a value of $250,000 or more.
- All "complex" one- to four-family residential property appraisals rendered in transactions of $250,000 or more. Institutions must determine whether the appraisal required is complex. If during the course of the appraisal a licensed appraiser identifies factors that would result in the property, form of ownership, or market conditions being considered atypical, then the appraisal would be viewed as complex and the institution may either: (1) ask the licensed appraiser to complete the appraisal and have a certified appraiser approve and cosign the appraisal or (2) engage a certified appraiser to complete the appraisal.

A state-licensed or state-certified appraiser must prepare an appraisal in the following circumstance:

- All transactions with values greater than $100,000 that do not require the use of a state-certified appraiser.

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) established December 31, 1992, as the date by which federally regulated depository institutions must use state-certified or state-licensed appraisers to complete appraisals on federally related transactions.

Appraisals Not Required

The appraisal rule requires state-certified or licensed appraisers, as appropriate, to be used for all real estate-related financial transactions except those transactions in which one or more of the following exemptions applies:

- The transaction value is less than or equal to $100,000.

- A lien is placed on real property as collateral solely through an abundance of caution and where the terms of the transaction as a consequence have not been made more favorable than they would have been in the absence of a lien.

- The transaction involves a lease of real estate that is not the economic equivalent of a purchase or sale.

- There is a transaction resulting from a maturing extension of credit, provided that:

  — The borrower has performed satisfactorily according to the original terms;

  — No new monies have been advanced other than what was previously agreed;

  — The credit standing of the borrower has not deteriorated; and

  — There has been no obvious and material deterioration in market conditions or physical aspects of the property that would threaten the institution's collateral protection.

- A regulated institution purchases a loan or interest in a loan, pooled loan, or interests in real property, including mortgage-backed securities, provided that there was an appraisal prepared for each pooled loan or real property interest that met the requirements of the regulation, if applicable, at the time of origination.

Appraisal Content

Appraisals should contain sufficient supporting documentation to enable the reader to understand appraiser's logic, reasoning, judgment, and analysis in reaching a final estimate of value.

The following are the minimum standards for appraisals for federally related transactions.

- Appraisals must conform to the USPAP adopted by the Appraisal Standards Board of the Appraisal Foundation (except for the Departure Provision, which savings associations cannot use). Appraisals must explain steps taken to comply with the Competency Provision of the USPAP.

- Appraisals shall be written and presented in a narrative format or on forms that satisfy the requirements of § 564.4.

- Appraisals must be based on the definition of market value found in § 564.2(f).

    — Appraisals should be sufficiently descriptive to enable both the savings association's personnel and regulatory staff to ascertain the estimated market value and the rationale for the estimate by providing detail and depth of analysis that reflects the complexity of the real estate appraised. Appraisals must contain sufficient supporting documentation so that the appraiser's logic, reasoning, judgment, and analysis in arriving at a conclusion indicate to the reader the reasonableness of the market value reported. For example, any current agreement of sales, option, or listing of the property should be analyzed and reported, if this information is available to the appraiser.

    — All appraisal reports must include the market value of the property on the appraisal date. For appraisals of properties where a portion of the overall real property rights or physical assets would typically be sold to the ultimate user(s) over time, reports should include: (1) market value of the property and interest "as is" on appraisal date, (2) market value "as if complete" on appraisal date, and (3) prospective future value of the property and interest upon completion of construction. For appraisals of properties where market conditions indicate that stabilized occupancy is not likely upon completion, reports should include: (1) market value "as is" on appraisal date, (2) prospective future value upon completion of construction, and (3) prospective future value upon reaching stabilized occupancy on the projected date of stabilization.

    — Appraisals should analyze and report data on current revenues, expenses, and vacancies for the property if it is and will continue to be income-producing. For these existing income-producing properties, appraisals should include actual profit and loss statements, or a statement indicating that such statements are unavailable, and a projection of future operating performance. Current rents and occupancy levels should also be reported.

    — Appraisal reports should also contain an estimate of the subject property's highest and best use, regardless of whether the actual or proposed use is the highest and best use.

    — Appraisal reports for proposed projects should be identified, dated and based upon the most recent plans and specifications. For proposed construction, development, or changes in use of a property, the appraisal report should address the project's economic feasibility. (If a feasibility study is used that was prepared by another party, the appraiser should explain the reasoning for accepting or rejecting the study). Appraisals should analyze and report on current market conditions and trends that will affect projected income or the absorption period, to the extent they affect the value of the subject property. Appraisals must analyze and report deductions and discounts (such as holding costs, marketing costs, entrepreneurial profit, leasing commissions, rent losses and tenant improvements) for any proposed construction, any completed properties that are partially leased or leased at other than market rents as of the date of the appraisal, and any tract developments or projects with unsold units.

— Appraisals must follow a reasonable valuation method that addresses the direct sales comparison, income, and cost approaches to market value, reconciles those approaches, and explains the elimination of each approach not used.

— For the direct sales comparison approach, appraisal reports should contain sufficient information to demonstrate that the comparison transactions were conducted under terms and conditions similar to the proposed transaction. The selected properties should be physically and economically comparable with the subject property, and any adjustments made should be sufficiently explained, including how the adjustment amounts were determined.

- Appraisals must analyze and report in sufficient detail any prior sales of the property being appraised that occurred within the past twelve months for one- to four-family residential properties and the past three years for all other properties. A longer history of comparable sales should be analyzed and reported when such properties have been sold several times over a brief period or when sales prices of such properties have increased or decreased at a significant rate.

- Appraisals should analyze and report a reasonable marketing period for the property.

- Appraisals must identify and separately value any personal property, fixtures, or intangible items that are not real property but that are included in the appraisal and discuss the effect of their inclusion or exclusion on the estimate of market value.

- Appraisals must include in the certification required by the USPAP an additional statement that the appraisal assignment was not based on a requested minimum valuation, a specific valuation, or the approval of a loan.

- Appraisals must include a legal description of the real estate being appraised, in addition to the description required by the USPAP.

- The appraisal should disclose and explain any unavailable pertinent or required information, as well as the date of the value estimates and the date of the report.

- Appraisal reports should contain a certification that states: (1) that the appraiser has no present or prospective interest in the subject property or the parties involved, (2) whether the appraiser made a personal inspection of the subject property, and (3) that to the best of the appraiser's ability, the analyses, opinions, and conclusions were developed and the report was prepared in accordance with the savings association's appraisal standards.

Appraisal Forms

Part 564 of the OTS regulations permits appraisals to be completed on OTS-approved forms that satisfy the requirements of the regulation. Approved forms include those approved by the Federal Home Loan Mortgage Corporation (FHLMC) and the Federal National Mortgage Association (FNMA) for existing or proposed one- to four-family residential properties or existing multifamily properties.

FHLMC and FNMA forms are not to be used for proposed tract developments. In addition, on December 3, 1990, OTS announced the availability of a revised commercial/industrial appraisal report form for existing property and a new form for small commercial/industrial property with associated instruction manuals. These forms are available from the Appraisal Foundation, Washington, D.C. For appraisals presented in a narrative format, the requirement for a sales history is waived if such history is unobtainable, and the appraiser certifies that in the report.

Evaluations

Certain real estate-related transactions are exempt from the requirement of Part 564 that a certified or licensed appraiser perform the appraisal. Real estate-related financial transactions that do not require an appraisal include loans of $100,000 or less. Consistent with the regulation, however, those transactions that do not require an appraisal must receive an evaluation of the real estate collateral that reflects prudent lending practices and OTS policies and guidelines.

For transactions that do not require an appraisal by a licensed or certified appraiser under the appraisal regulations, an institution is required to establish, as a prudent practice, an evaluation program and perform an appropriate evaluation of the real estate. The evaluation should result in a determination of value that will assist the institution in assessing the soundness of the transaction and that will protect an institution's interest in the transaction.

An evaluation need not meet all of the detailed requirements of an appraisal as set forth in Part 564. File documentation should, however, support the estimate of value and include sufficient information for an individual to fully understand the evaluator's analysis. The evaluation should describe the property and its location, and discuss its use, especially if it is nonresidential. The evaluation should include the evaluator's calculations, supporting assumptions for the estimate of value, and, if applicable, a discussion of comparable property values. An evaluation must be written, signed, dated, and include the preparer's name and address. To qualify, an evaluator must be capable of rendering unbiased estimates of value and must have real estate-related training or experience relevant to the type of property.

The scope of an evaluation should be consistent with the complexity of the transaction and type of real estate collateral. An evaluation that supports a more complex transaction generally needs a more detailed analysis. An evaluation for a less complex transaction will generally require a less detailed analysis, and may be based upon information such as the current tax assessed value or comparable property sales from sales data services, such as the multiple listing service. The institution may use its own real estate loan portfolio experience and appraisals prepared in accordance with Part 564 for loans on comparable properties as a basis for an evaluation.

These supervisory guidelines do not preclude an institution from obtaining an appraisal that conforms to the appraisal regulations for any real estate-related financial transaction. For institutions that make loans that may be sold into the secondary market at a later date, the appraisals obtained should meet secondary mortgage market requirements.

Useful Life of Appraisals or Evaluations

An institution should establish criteria to determine whether an existing appraisal or evaluation continues to be valid to support a subsequent transaction. The useful life of an appraisal or evaluation will vary depending upon the circumstances of the property and the market place. An institution's management should determine if there have been material changes to the underlying assumptions in the appraisal or evaluation that affect the original estimate of value.

Examples of factors that could cause material changes to reported values include: the passage of time; the volatility of the local market; the availability of financing; the inventory of competing properties; new improvements to, or lack of maintenance of, the subject property or competing surrounding properties; a change in zoning; or environmental contamination. If the useful life of an appraisal or evaluation has lapsed, an institution should determine whether there is a need to reappraise or reevaluate the real estate.

Reappraisals and Reevaluations

An institution's real estate appraisal and evaluation programs should also include safety and soundness considerations that identify when it is in the institution's interests to reappraise or reevaluate real estate collateral. Some of these considerations are the condition, performance, quality and status of the loan, and the strength of the underlying collateral. In problem situations, such as loan workouts, renewals, or restructurings, or troubled real estate loans, when the institution is more dependent upon the real estate collateral, management should consider the prudence of a reappraisal or reevaluation of the collateral.

Management should also be guided by the November 7, 1991 "Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans" on this issue.

Institutions should document information sources and analyses used to determine the validity of an existing appraisal or evaluation. Reappraisals and reevaluations of collateral must comply with Part 564 and Thrift Bulletin 55 (TB 55), Real Estate Appraisal and Evaluation Guidelines.

Updated Appraisals

An updated appraisal is currently not an acceptable appraisal as defined by Part 564. An institution may, however, use an updated appraisal: (1) to evaluate real estate not subject to the appraisal requirements in Part 564 and (2) to assess the useful life of an appraisal.

Depository Institutions Disaster Relief Act of 1992

Section 2 of the Depository Institutions Disaster Relief Act of 1992 (DIDRA), signed by the President on October 23, 1992, authorizes the federal bank regulatory agencies to make exceptions to statutory and regulatory requirements relating to appraisals for certain transactions. The exceptions are available for transactions that involve real property in major disaster areas when the exceptions would facilitate recovery from the disaster and would not be inconsistent with safety and soundness. Any such exceptions expire not later than three years after the disaster is declared by the President. On November 23, 1992, the OTS, along with the bank regulatory agencies, determined that recovery from

Hurricanes Andrew and Iniki and from the Los Angeles Civil Unrest in May 1992 would be facilitated by excepting transactions involving real estate located in the areas directly affected by those disasters from the appraisal requirements of Part 564. A similar exception was granted for the areas affected by the extensive flooding in the Midwest on August 11, 1993 and areas affected by the earthquake in Southern California on February 11, 1994.

While the purpose of § 2 of DIDRA is to remove the impediment to depository institutions making loans and engaging in other transactions that would help to finance reconstruction and rehabilitation of affected areas, the Act does not excuse management from its obligation to ensure that safety and soundness are not compromised by such activity. Lenders should document that the loan will facilitate reconstruction and rehabilitation of the disaster. Loans should be prudently underwritten and contain the best estimate of value available.

Regulator evaluation of specific loans and lending programs should focus on the overall quality of the assets, including loan documentation that supports those assets with unique or unusual circumstances. Regulators should consider any special circumstances that exist and the efforts of the institution to work with borrowers to reconstruct and rehabilitate the community.

Relief under § 2 of DIDRA for areas affected by disasters other than those described in the November 23, 1992, August 11, 1993, and February 11, 1994, orders are only available upon issuance of an order by the OTS Director. If there is a need for such relief in a region, the regional director should submit a request that the Director issue such an order pursuant to the authority provided by § 2 of DIDRA.

Proposed Regulation

On June 4, 1993, the federal bank regulatory agencies published a proposal to revise the appraisal rule. The proposed revisions would increase to $250,000 the threshold level at or below which appraisals are not required and identify additional circumstances when appraisals are not required. In the proposal, the OTS stated that it would, as a matter of policy, require problem institutions or institutions in a troubled condition to obtain appraisals for transactions of more than $100,000. In addition, the proposal would amend existing requirements governing appraisal content and appraiser independence. Specifically, the proposal seeks to remove most of the additional standards currently required by the appraisal regulation in § 564.4 and require only the following:

- Conform to the USPAP adopted by the Appraisal Standards Board of the Appraisal Foundation;
- Be written;
- Set forth a market value; and
- Be performed by state-licensed or certified appraisers in accordance with requirements set forth in the appraisal regulation.

Also, the agencies proposed to amend the appraisal regulations to permit use of appraisals prepared for financial services institutions other than institutions subject to Title XI of FIRREA (nonregulated institutions). This would include appraisals prepared for mortgage bankers. The appraiser would not be allowed to have a direct or indirect interest, financial or otherwise, in the property or the transaction, and must have been directly engaged by the nonregulated institution. Further, the regulated institution would be required to ensure that the appraisal conforms to the requirements of the regulation and is otherwise acceptable.

Proposed Exemptions

Under the proposed rule published on June 4, 1993, the services of a state-certified or licensed appraiser would not be necessary for the following real estate-related financial transactions:

- The transaction value is $250,000 or less;
- The transaction is not secured by real estate;
- A lien on real estate has been taken for purposes other than the real estate's value;
- The transaction is a business loan that: (1) has a transaction value of less than $1 million and (2) is not dependent on the sale of, or rental income derived from, the real estate taken as collateral as the primary source of repayment;
- The transaction is insured or guaranteed by a United States government agency or United States government-sponsored agency;
- The transaction meets all of the qualifications for sale to a United States government agency or United States government-sponsored agency;
- The regulated institution is acting in a fiduciary capacity and is not required to obtain an appraisal under other law; or
- The OTS determines that the services of an appraiser are not necessary in order to protect federal-financial and public policy interest in real estate-related financial transactions or to protect the safety and soundness of the institution.

The proposed rule would also modify certain of the existing exceptions so that appraisals would not be required when:

- A lien on real estate has been taken as collateral in an abundance of caution;
- The transaction results from an existing extension of credit, provided that there is no obvious or material deterioration in market conditions or physical aspects of the property that threaten the institution's real estate collateral protection; or

- The transaction:

  — involves the purchase, sale, investment in, exchange of, or extension of credit secured by a loan or interest in a loan, pooled loans, or interests in real property, including mortgaged-backed securities; and

  — is supported by an appraisal that meets the requirements of Part 564 for each loan or interest in a loan, pooled loan, or real property interest originated after August 24, 1990.

Under the proposed regulation, transactions under $250,000; business loans with a transaction value less than $1 million that are not dependent upon sale or rental income from the property for repayment; and transactions resulting from existing extensions of credit should have an appropriate evaluation of the real estate collateral that is consistent with TB 55 and other supervisory guidance.

Supervisory Considerations

Regulators will review an institution's real estate appraisal and evaluation policies, programs, and procedures as part of the examination process. Regulators will consider the institution's size and the nature of its real estate-related activities in their assessment of the appropriateness of its programs.

In the analysis of individual transactions, regulators will review appraisals or evaluations to determine that the methods, assumptions, and findings are reasonable and in compliance with Part 564. In addition, regulators will review the steps taken by an institution to ensure that the individuals who perform its appraisals or evaluations are qualified and are not subject to any conflicts of interest.

Failure to establish and maintain acceptable programs or to comply with applicable regulations and policies is considered an unsafe and unsound practice. Institutions will be required to correct violations and deficiencies detected in their appraisal and evaluation practices. Appraisers should be independent of the borrower and seller, and of the loan underwriting and collection functions. Beginning January 1, 1993, appraisers must be certified or licensed by their respective states.

Use of Appraisals

Management is responsible for reviewing each appraisal's assumptions and conclusions for reasonableness. Appraisal assumptions should not be based solely on current conditions that ignore the stabilized income-producing capacity of the property. As stated in the November 7, 1991, "Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans," management should adjust any assumptions used by an appraiser in determining value that are overly optimistic or pessimistic. This review and any resulting adjustments to value are solely for management's use and do not involve actual adjustments to an appraisal.

A regulator should analyze the collateral's value as determined by the institution's most recent appraisal or evaluation. A regulator should review the major facts, assumptions and approaches used by the appraiser (including any comments made by management on the value rendered by the appraiser). Under certain circumstances, the regulator may make adjustments to this assessment of value. This review and any resulting adjustments to value are solely for purposes of a regulator's analysis and classification of a credit and do not involve actual adjustments to an appraisal.

If a regulator concludes that an appraisal or evaluation is deficient for any reason, that fact should be taken into account in reaching a judgment on the quality of the loan or investment. In addition, as discussed in the November 7, 1991, "Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans," the estimated value of the underlying collateral may be adjusted for credit analysis purposes when the regulator can establish that any underlying facts or assumptions are inappropriate and the regulator can support alternative assumptions. It is important to emphasize that a regulator's overall analysis and classification of a loan or investment may be based upon other credit or underwriting standards, even if the loan or investment is secured by real property whose value is supported by an appraisal or evaluation.

Corrective Actions

When regulators find substantial indications of unacceptable appraisal practices, they should discuss their findings with the caseload manager and the regional appraisal staff to initiate corrective action. Examples of unacceptable practices include fraudulent omission of critical information, misleading assumptions, manipulation of data to create an unjustified conclusion, ignoring environmental risk, acceptance of compensation contingent upon reporting a predetermined value, and conflicts of interest.

In some instances, review of appraisal reports by the regional appraiser may be appropriate. When examination findings disclose substantial indications of poor appraisal practice, the regional appraiser, with the approval of the regional deputy director, is authorized to refer appraisers to either: (1) the state licensure/certification authority or (2) the professional societies of which the appraiser is a member. The regional appraiser, with the approval of the regional deputy director, is further authorized to request societies to review the subject appraisal reports that prompted the reference. A copy of referral requests originating at each region should be sent to the OTS Appraisal Subcommittee Member, the FFIEC Appraisal Subcommittee, and the Washington Deputy Chief Counsel for Enforcement. The memorandum should describe the basis for referral, identify the security property, identify all appraisers involved, state the professional societies of which each appraiser is a member, and indicate the date of each appraisal report.

In connection with the examination of savings associations, a regional director is authorized to obtain appraisal reports for real estate securing a savings association's loans. The regional director, or designee, may require appraisals of real estate owned (REO) when considered necessary.

Supervisory Review Process

OTS Regulatory Bulletin 4a (RB 4a), "Supervisory Review Process," contains an informal process for reviewing adverse supervisory and examination decisions. Among the decisions subject to review is the appraised value of any property serving as collateral to secure the repayment of any loan held by the claimant. Institutions are encouraged to raise examination-related disagreements that cannot be resolved during the examination with the regional office. A supervisory decision in dispute may be raised either orally or in writing to the assistant director, regional deputy director, or regional director.

The regional office will act within 30 days of receipt of an appeal. If no satisfactory resolution results, an appeal may be filed with the Deputy Director of Regional Operations, Washington, D.C.

REFERENCES

Code of Federal Regulations

Subchapter B: Consumer-Related Regulations

§ 528.2a	Nondiscriminatory Appraisal and Underwriting

Subchapter C: Regulations for Federal Savings Associations

§ 545.32	Real Estate Loans
§ 545.40	Loans on Low-Rent Housing

Subchapter D: Regulations Applicable to all Savings Associations

§ 563.170(b)	Appraisals
§ 563.172	Re-evaluation of Real Estate Owned
Part 564	Appraisals
§ 571.20	Payment for Appraisals

Office of Thrift Supervision Bulletins

RB 4a	Supervisory Review Process
TB 55	Real Estate Appraisal and Evaluation Guidelines

Comment-Rulings

87-1295	Regulations Re Preamble Appraisal Policies and Practices of FSLIC-Insured Institutions and Service Corporations

Other

Interagency Policy Statement on the Review and Classification of Commercial Real Estate Loans (November 7, 1991)

Uniform Standards of Professional Appraisal Practice (USPAP)