

July 19, 2018

The Honorable Steve Chabot
Chairman
House Committee on Small Business
United States House of Representatives
231 Rayburn House Office Building
Washington, DC 20515

The Honorable Nydia Velazquez
Ranking Member
House Committee on Small Business
United States House of Representatives
2302 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Chabot and Ranking Member Velazquez:

On behalf of more than 18,000 members of the largest organization of professional real property appraisers, the Appraisal Institute writes to express our strong concern with H.R. 6347, the “7(a) Real Estate Appraisal Harmonization Act”, and H.R. 6348, the “Small Business ACE Act”, both of which adjust upward the real estate appraisal thresholds for major SBA Loan programs.

HR 6347/HR 6348 would peg the SBA appraisal threshold level to the threshold level established by the federal bank regulatory agencies (the Agencies). Earlier this year, those Agencies issued a final rule to increase the commercial real estate appraisal threshold level to \$500,000, up from \$250,000. The SBA appraisal threshold level is found in statute and currently stands at \$250,000. After introducing the bills on July 12, the House Committee on Small Business favorably reported the bills on July 18 to attempt to align or harmonize the SBA requirements with those of the Agencies.

As background, the so called “agency exemption” established by the federal bank regulatory agencies in 1994 and utilized by the SBA is predicated on an assumption that the agency issuing loan guarantees has a sufficient real estate appraisal program in place consistent with the final rule on Real Estate Appraisals¹. When the Agencies issued the final rule earlier this year establishing a \$500,000 commercial real estate appraisal threshold level, the Agencies also required the performance of an “evaluation” prepared in accordance with the Interagency Appraisal and Evaluation Guidelines². Generally, evaluations should contain sufficient information and analysis to support the financial institution’s decision to engage in the transaction and can be prepared by appraisers but may be prepared by others with real estate knowledge and experience.

Current SBA requirements do not include a requirement for the performance of evaluations where an appraisal is not required by the agency. So, in effect, HR 6347/HR6348 “cherry picks” the increase in the threshold level, overlooking the requirement to prepare an evaluation. This is a dangerous omission given wide latitude granted to non-banks and nonprofit organizations in ordering appraisals within the SBA program, where collateral valuation policies and procedures are likely not to be as robust as those of federally regulated institutions and where concerns about the independence of the appraisal process may be paramount. In fact, our members, including those overseeing SBA appraisal orders within federally regulated financial institutions, have expressed concern to us about the quality of appraisals ordered by non-bank institutions, so much so, that many regulated banks refuse to accept appraisals ordered by such entities.

¹ <https://www.occ.treas.gov/news-issuances/federal-register/94fr13312.pdf>

² *For commercial real estate transactions exempted from the appraisal requirement as a result of the revised threshold, regulated institutions must obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices.*
<https://www.federalregister.gov/documents/2018/04/09/2018-06960/real-estate-appraisals>

The Agencies urge regulated institutions to obtain appraisals even below the threshold level where there are borrowers with high risk characteristics – the very situation that SBA caters to. Specifically, the Interagency Appraisal and Evaluation Guidelines state:

Although the Agencies’ appraisal regulations allow an institution to use an evaluation for certain transactions, an institution should establish policies and procedures for determining when to obtain an appraisal for such transactions. For example, an institution should consider obtaining an appraisal as an institution’s portfolio risk increases or for higher risk real estate-related financial transactions, such as those involving:

- *Loans with combined loan-to-value ratios in excess of the supervisory loan-to-value limits.*
- *Atypical properties.*
- *Properties outside the institution’s traditional lending market.*
- *Transactions involving existing extensions of credit with significant risk to the institution.*
- *Borrowers with high risk characteristics³.*

Further, we caution on relying too heavily on the perceived health of the SBA loan portfolios as substantiation for loosening risk management requirements. There is much that goes into the SBA default rate, in fact, as the agency does not always take a loss where others do. The agency provides loan guarantees, but if a lender makes a mistake, the SBA does not honor the guarantee (or reduces it significantly). The SBA does not let a bank cite or take action against a borrower if they do not meet basic covenants (e.g. providing annual financial statements). According to at least one recent estimate, as many as 1 in 6 SBA loans defaulted in recent years⁴. Recent steps taken by the Committee to urge more enhanced credit risk management by the SBA are a positive step forward, but that should also include strengthened collateral risk management requirements. Failing to include an evaluation requirement would result in a significant step backwards in this area, in our view.

In the end, if the goal of this legislation is to “harmonize” the SBA requirements with those of the Agencies, an evaluation requirement should also be included. Given the risks involved in SBA lending, we believe this should also include incentives for SBA lenders to utilize appraiser-prepared evaluations by providing regulatory relief to appraisers providing such services. While this would not eliminate our concern about increasing taxpayer risk, it would help to lessen it all things considered.

Beyond this, there are other areas of SBA appraisal policy that could benefit from harmonization with the requirements of the Agencies. In recent years, the agency has grappled with requirements for special purpose properties, for example, where lessons can be learned from the conventional market and the experiences of practitioners, regulated institutions, and bank examiners. Matters like this would benefit from further study and stakeholder input, and in our view, would be wholly consistent with the goal of reducing “red tape” and harmonizing requirements.

We look forward to working with you to address these and other concerns as the full House considers the bills and are reviewed by the Senate. Please contact Bill Garber, Director of Government Relations for the Appraisal Institute, at 202-292-5586 or bgarber@appraisalinstitute.org, or Brian Rodgers, Manager of Government Relations, at (202) 298-5597 or brodgers@appraisalinstitute.org should you like to arrange a meeting or have any questions.

Thank you in advance for your consideration.

Sincerely,

Appraisal Institute

³ <https://www.fdic.gov/regulations/laws/rules/5000-4800.html>

⁴ <https://www.nerdwallet.com/blog/small-business/sba-lending-trends-match-consumer-tastes/>