



FEDERAL RESERVE BANK *of* KANSAS CITY

March 24, 2016

**Supervision and Regulation (SR) Letter 16-5: Interagency Advisory on the Use of Evaluations in Real Estate-related Financial Transactions**

**Attention:** Chief Executive Officer of Each Tenth District State Member Bank and Holding Company

**In Brief:** The Federal Reserve, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (the agencies) have jointly issued an advisory statement to remind financial institutions of existing regulatory guidance on the use of evaluations instead of appraisals for estimating the market value of real property securing real estate-related financial transactions.

**Highlights:** In outreach meetings conducted by the agencies pursuant to the Economic Growth and Regulatory Paperwork Reduction Act, the agencies received many questions pertaining to the circumstances under which evaluations may be used in the underwriting of real estate-related transactions and how to support a market value conclusion when there have been few or no recent comparable sales. This advisory statement is meant to address those questions by describing existing supervisory expectations, guidance and industry practices.

Agency regulations require an appraisal to be completed by a competent and qualified state-licensed or state-certified appraiser that complies with the Uniform Standards for Professional Appraisal Practice for any real estate-related financial transaction, unless an exception exists. The statement offers a sample of exceptions when an evaluation may be used in the place of an appraisal. Exceptions include but are not limited to: transactions where the loan amount is less than \$250M; and real estate-secured business transactions where the loan amount is less than \$1,000M and the note does not rely on the sale of or rental income from real estate as the primary source of repayment.

The advisory statement also discusses who is qualified to prepare an evaluation. While the preparer does not need to be state-licensed or certified, he or she should be knowledgeable, competent and independent of the transaction and loan production function. Bank employees or third parties are acceptable reviewers in smaller communities. The preparer may consider using one or more valuation approaches to reach a reliable estimate of the property if the approaches are appropriate for the property being evaluated. While the sales comparable approach is the most commonly used method of valuation, in areas where there have been few recent or comparable sales the preparer may use other approaches such as cost or income.

While there is no standard format for documenting the information or analysis performed to determine the market value in the evaluation, the statement concludes that regardless of the approach used, the evaluation should contain sufficient information to allow a reader to understand the analysis that was performed to support the conclusion.

**Contact:** Please direct any questions concerning the new guidance to your Federal Reserve Bank of Kansas City central point of contact at (800) 333-1010.

**Internet Link:** A copy of the Federal Reserve Supervision and Regulation Letter SR 16-5 is available on the Board's public web site at: <http://www.federalreserve.gov/bankinfo/srletters/sr1605.htm>