



## Financial Services & Products ADVISORY ■

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### Federal Minimum Standards for Appraisal Management Companies Approved

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Just over a year after their proposal, late last month six federal regulatory agencies—the Office of the Comptroller of the Currency (OCC), Federal Reserve Board (FRB), Federal Deposit Insurance Corporation (FDIC), National Credit Union Administration (NCUA), Consumer Financial Protection Bureau (CFPB) and Federal Housing Finance Agency (collectively, the “agencies”)—approved rules creating federal minimum requirements for state registration and supervision of appraisal management companies (“minimum standards”). The final rule implements Section 1473 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which added Section 1124 to the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) to include requirements for appraisal management companies (AMCs). Noteworthy is that according to the agencies,

Section 1124 does not compel a State to establish an AMC registration and supervision program, nor is a penalty imposed on a State that does not establish a regulatory structure for AMCs within 36 months of issuance of this final rule. However, *in a State that has not adopted the AMC minimum requirements established by this rule, AMCs are barred by section 1124 from providing appraisal management services for Federally related transactions, unless they are owned and controlled by a Federally regulated depository institution.*<sup>1</sup>

The final rule will take effect 60 days after publication in the *Federal Register* (the date of which is to be determined); states will have three years from the rule’s effective date to implement the minimum standards (with the possibility of a one-year extension). Federally regulated AMCs will have 12 months from the rule’s effective date to comply with applicable requirements.

<sup>1</sup> Emphasis added.

## What Do the Minimum Standards Do?

### *Set a baseline*

Unchanged from the proposed version of the rules, under the minimum standards each state that chooses to participate must have an AMC licensing program that meets certain criteria and must impose certain requirements on an AMC subject to state registration.<sup>2</sup> A state's AMC licensing program must have mechanisms to (1) review and approve or deny an AMC's application for initial registration; (2) review and renew or deny an AMC's registration periodically; (3) examine the books and records of an AMC operating in the state and require such AMC to submit reports, information and documents; (4) verify that appraisers on the AMC's panel hold valid state certifications or licenses, as applicable; (5) conduct investigations of AMCs to assess potential violations of applicable appraisal-related laws, regulations or orders; (6) discipline AMCs that violate applicable appraisal-related laws, regulations or orders; and (7) report an AMC's violation of applicable appraisal-related laws, regulations or orders, as well as disciplinary and enforcement actions and other relevant information about an AMC's operations, to the Appraisal Subcommittee.<sup>3</sup>

All AMCs subject to state registration must satisfy the following minimum standards:

1. Register with and be subject to supervision by the state appraiser regulator;
2. Engage only state-certified or state-licensed appraisers for federally related transactions (FRTs);
3. Establish and comply with processes and controls designed to ensure that an AMC only engages an appraiser who has the appropriate education, expertise and experience necessary to competently complete a particular appraisal assignment;
4. Direct the appraiser to perform the assignment in accordance with the Uniform Standards of Professional Appraisal Practice (USPAP); and
5. Establish and comply with processes and controls reasonably designed to ensure that the AMC conducts its appraisal management services in accordance with the appraisal independence standards of Section 129E(a)–(i) of the Truth in Lending Act (TILA) and regulations adopted thereunder.<sup>4</sup>

States remain free to impose additional obligations on registered AMCs, as Section 1124 of FIRREA is not intended to “be construed to prevent States from establishing requirements in addition to” the minimum standards.

**Alston & Bird Observation:** Those who had hoped that the minimum standards would provide some consistency in the 50-state regulatory landscape may be disappointed. Once they meet the baseline, states are free to create additional requirements for AMCs—which, as they exist in current laws, may be vastly inconsistent. For instance, in the final rule the agencies declined to provide guidance on whether and how states may interpret and enforce the “customary and reasonable” fee provision of Section 129E of TILA—an issue that has troubled AMCs in recent years.

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<sup>2</sup> See 12 C.F.R. § 34.213. For brevity of reference, citations are to the OCC rules, the first that appear in the planned *Federal Register* notice.

<sup>3</sup> *Id.* § 34.213(a).

<sup>4</sup> *Id.* § 34.213(b).

### **Clarify the entities to which their requirements apply**

When proposing the minimum standards, the agencies sought comment on how to define the terms “appraisal management company” and “appraisal management services.”

As adopted, the agencies’ rules define an AMC as a person that: (1) provides appraisal management services to creditors or secondary mortgage market participants, including affiliates; (2) provides such services in connection with valuing a consumer’s principal dwelling as security for a consumer credit transaction or incorporating such transactions into securitizations; and (3) within a given 12-month period oversees an appraisal panel of more than 15 state-certified or state-licensed appraisers in a state or 25 or more state-certified or state-licensed appraisers in two or more states.<sup>5</sup>

The definition of AMC turns on the term “appraisal management services,” which means one or more of the following: (1) recruiting, selecting and retaining appraisers; (2) contracting with state-certified or state-licensed appraisers to perform appraisal assignments; (3) managing the process of having an appraisal performed, including providing administrative services such as receiving appraisal orders and appraisal reports, submitting completed appraisal reports to creditors and secondary market participants, collecting fees from creditors and secondary market participants for services provided, and paying appraisers for services performed; and (4) reviewing and verifying the work of appraisers.<sup>6</sup>

**Alston & Bird Observation:** Based on the final definitions of “appraisal management company” (which, as in its proposed form, does not include the direct performance of appraisals) and of the consideration only of independent contractors when determining panel membership, the minimum standards exclude appraisal firms from their scope (an issue on which the agencies had requested comment).<sup>7</sup> This puts appraisal firms at a competitive advantage as their regulatory compliance burdens will be significantly lower than state regulated AMCs, and they will have the ability to perform FRTs in every jurisdiction. Hybrid entities (those utilizing both employee and independent contractor appraisers to perform services) will be subject to the minimum standards only “when the entity maintains a panel of appraisers that includes independent contractors meeting the threshold minimum numbers.” The agencies declined to treat the definitions of “AMC” and “appraisal management services” as a minimum standard. As a result, although states may not reduce the range of services that would classify an AMC, they may establish additional requirements in these definitions. With regard to portals—entities that provide appraisal-related services through electronic means—the agencies declined to state that they are not AMCs. Rather, the agencies state, “The business model an entity uses to provide services should not be determinative of whether the entity is an AMC; rather, if a portal is providing appraisal management services, and meets the other elements of the definition, then it should be considered an AMC under the final rule.”

<sup>5</sup> *Id.* § 34.211(c)(1). Only independent contractors (as that term is defined for federal income taxation purposes) are to be included when calculating the size of an AMC’s appraiser panel.

<sup>6</sup> *Id.* § 34.211(d).

<sup>7</sup> According to the commentary to the minimum standards, the agencies distinguish appraisal firms from AMCs “for three key reasons”: (1) Section 1472 of the Dodd-Frank Act, which identified certain entities to be excluded from the coverage of the minimum standards, describes an entity that utilizes the services of state-certified or state-licensed appraisers and “receives a fee for performing appraisals”; (2) Section 1124 of FIRREA uses the term “appraisal management company,” but does not make specific reference to the term “appraisal firm”; and (3) Section 1121 of FIRREA describes the activities of AMCs as including contracting with state-certified or state-licensed appraisers, but not directly performing appraisals, whereas the agencies understand the direct performance of appraisals to be a key activity of appraisal firms.

**Identify “federally regulated AMCs” to which different of the minimum standards apply**

A “federally regulated AMC,” meaning an AMC that is owned and controlled by an insured depository institution, as defined in 12 U.S.C. § 1813, and regulated by the OCC, FRB or FDIC,<sup>8</sup> is subject to all of the state requirements discussed above, except the requirement to register with a state.

**Alston & Bird Observation:** Despite requests from commenters, the agencies did not define or otherwise provide guidance on the term “owned and controlled.” As a result, the standard for determining which entities will be considered “federally regulated AMCs” remains unclear.

**Determine the size of an AMC’s appraiser panel**

Key to the determination of what entities qualify as an AMC, as well as to other provisions of the minimum standards, are the definition of and rules relating to appraiser panel membership.

First, the agencies define “appraiser panel” as “a network, list or roster of licensed or certified appraisers approved by the AMC to perform appraisals as independent contractors for the AMC.”<sup>9</sup> (Independent contractor is defined according to how the AMC treats individuals for federal income taxation purposes.)

Second, the definition of AMC captures an entity that “[w]ithin a given 12-month period... oversees an appraiser panel of more than 15 State-certified or State-licensed appraisers in a State or 25 or more State-certified or State-licensed appraisers in two or more States.” Pursuant to that requirement, the final rule provides guidance on the annual size calculation of an AMC’s appraiser panel. Specifically, an appraiser is deemed to be part of an AMC’s appraiser panel as of the earliest date on which the AMC: (1) “[a]ccepts the appraiser for the AMC’s consideration for future appraisal assignments in covered transactions or for secondary mortgage market participants in connection with covered transactions; or (2) [e]ngages the appraiser to perform one or more appraisals on behalf of a creditor for a covered transaction or secondary mortgage market participant in connection with covered transactions.”<sup>10</sup>

Third, an appraiser remains part of an AMC’s appraiser panel until the AMC: (1) sends written notice removing the appraiser from its panel and explaining the reason for such action; or (2) receives written notice from the appraiser requesting removal, or notice of the appraiser’s death or incapacity.<sup>11</sup> However, an appraiser who is removed from a panel and subsequently added again within a 12-month period “will be deemed to have been part of the AMC’s appraiser panel without interruption.”<sup>12</sup>

Finally, the final rule leaves it to the states to determine on what basis the 12-month period will be counted, whether by the calendar year or other means.<sup>13</sup>

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<sup>8</sup> *Id.* § 34.211(k). The agencies exclude credit union service organizations from the definition of “federally regulated AMCs” because such entities are not subject to oversight by the NCUA in the same manner that subsidiaries of banks and savings banks are subject to oversight by the financial institutions’ prudential regulators.

<sup>9</sup> 12 C.F.R. § 34.211(e).

<sup>10</sup> *Id.* § 34.212(a).

<sup>11</sup> *Id.* § 34.212(b).

<sup>12</sup> *Id.* § 34.212(c).

<sup>13</sup> *Id.* § 34.212(d).

**Alston & Bird Observation:** The agencies declined to incorporate the view of commenters who requested that only actively engaged appraisers be counted towards panel membership, in part out of concern that doing so would encourage attempts to evade registration. However, the resulting rule leaves open the possibility that AMCs may maintain vastly smaller panels in order to reduce costs, which could negatively impact rural areas and small communities where fewer appraisers may be available to complete assignments. However, the agencies note that Section 1121 of FIRREA references the number of appraisers that an AMC oversees on a panel or in a network, and not the number of appraisers to which it actually gives assignments. Furthermore, the agencies did not address the tie between panel membership and the payment of AMC National Registry fees to the Appraisal Subcommittee (ASC).

### ***Distinguish “covered transactions” from “federally related transactions”***

The minimum standards apply to AMCs providing services in connection with a “covered transaction,” meaning any consumer credit transaction secured by the consumer’s principal dwelling.<sup>14</sup> By contrast, as the agencies note, Title XI of FIRREA and its implementing regulations “have applied historically only to appraisals for [FRTs].” In adopting the minimum standards, the agencies take a broader approach, which they believe is “consistent with the structure and text of other parts of section 1124, most of which address appraisals generally rather than appraisals only for [FRTs].”

**Alston & Bird Observation:** In applying the minimum standards to consumer credit transactions secured by the consumer’s principal dwelling for both FRTs and non-FRTs, the application of the minimum standards is not limited to mortgage loan originations and thus may implicate servicing activity such as loan modifications. States may further expand the requirements to other credit transactions.

## **What Do the Minimum Standards Exclude?**

### ***A mandate for states to implement their requirements***

When proposing the minimum standards, the agencies set forth the idea that Section 1124 does not require the states to participate in their implementation. That idea carried through intact to the final rule. States have three years from the rule’s effective date to enact implementing legislation or to opt out of the minimum standards’ requirements. The final rule neither imposes a penalty for states that choose not to participate nor bars states from later enacting an AMC regime. However, in nonparticipating states, the only entities that will be able to provide appraisal management services in connection with FRTs are federally regulated AMCs and those that do not meet the panel membership threshold under the definition of an “appraisal management company.” (Notably, in applying only to FRTs, the restriction differs in scope from the minimum standards generally, which do not consider whether a covered transaction is an FRT.) The absence of a mandate has created considerable uncertainty for other AMCs—those that would be subject to state regulation—which face the possibility that a state may decline to create, or may repeal an existing, AMC regulatory scheme, thereby barring them from doing business in those states. Whether any of the 38 states that have enacted AMC laws will choose to comply with the minimum standards by repealing such laws, or whether any of the 13 holdouts will decide not to enact AMC legislation, will be resolved by 2018. However, even after the deadline for enactment of legislation, states will have the opportunity to elect to establish an AMC regulatory regime, again permitting AMCs to provide services in connection with FRTs.

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<sup>14</sup> *Id.* § 34.211(h).

**Alston & Bird Observation:** The minimum standards leave unanswered an interesting question: If states chose to adopt an appraiser licensing scheme, must they also adopt an AMC registration scheme? In the commentary, the agencies state that the minimum standards “apply to States that have elected to establish, pursuant to section 1117 of FIRREA, an appraiser certifying and licensing agency with authority to register and supervise AMCs.” Section 1117 provides in full:

To assure the availability of State certified and licensed appraisers for the performance in a State of appraisals in federally related transactions and to assure effective supervision of the activities of certified and licensed appraisers, a State may establish a State appraiser certifying and licensing agency. *The duties of such agency may additionally include the registration and supervision of the appraisal management companies and the addition of information about the appraisal management company to the national registry.*<sup>15</sup>

The permissive language of that section suggests that a state with an established, mandatory appraiser licensing program could choose not to register AMCs. Whether any states will choose that approach remains to be seen.

We note that in its economic impact analysis of the final rule, the CFPB “continues to rely on the assumption that the remaining States will choose to participate either within three years or soon thereafter” (and does not discuss the possibility of states opting out). Furthermore, even if states choose not to participate, the loans affected—portfolio loans over \$250,000 that are not insured by the Federal Housing Administration, Department of Veterans Affairs or Department of Agriculture Rural Housing Service—“represent a small percentage of the market, and therefore inability by certain market participants (certain types of AMCs) to provide appraisal management services in these types of transactions in a non-participating State will not result in a significant economic impact on a substantial number of small entities.” The note does not address the potential impact on larger entities.

#### ***Clarification on the ability of states to enforce the appraisal independence standards of Section 129E of TILA***

Comments on the agencies’ proposed rules included attention to the issue of whether states may interpret and enforce Section 129E of TILA, including the requirement for an AMC (as an agent of a creditor) to pay customary and reasonable rates of compensation to fee appraisers when services are being provided in connection with covered transactions. In the commentary to the minimum standards, the agencies decline to address the issue, stating that other than the mandate that states require AMCs to ensure that appraisals are conducted in accordance with Section 129E, “[q]uestions about what mechanisms a State agency may use to assess a party’s compliance in connection with any authority the State has to commence a civil action to enforce section 129E of TILA are outside the scope of this rulemaking.” Note that the Dodd-Frank Act expanded the enforcement authority of state attorneys general under Section 130(e) of TILA<sup>16</sup> to include Section 129E, but did not discuss whether state appraisal regulators may interpret that section through rulemaking or whether they may only enforce such interpretations by referring matters to their attorneys general.

**Alston & Bird Observation:** Given that the minimum standards incorporate a requirement for AMCs to comply with Section 129E of TILA, it is interesting that the agencies declined to opine on “what mechanisms a State agency may use to assess a party’s compliance in connection with any authority the State has to commence a civil action to enforce

<sup>15</sup> 12 U.S.C. § 3346 (emphasis added).

<sup>16</sup> 15 U.S.C. § 1640(e).

Section 129E of TILA.” Unless and until the agencies decide to address the issue, state appraisal boards appear to retain the ability to create and enforce their own interpretation of the customary and reasonable fee requirement—which has created considerable headaches for state-registered AMCs.

### ***A discussion of state standards for appraisal review by AMCs***

In their proposal, the agencies requested comment on whether and how to address issues regarding appraisal review. They emphasized that separate rulemaking on the issue would be required, pursuant to Section 1110 of FIRREA. That section requires the federal financial institution regulatory agencies to prescribe standards for the performance of real estate appraisals in connection with federally related transactions, including “that such appraisals shall be subject to appropriate review for compliance with the [USPAP].” Although the agencies acknowledge that Section 1121(11) of FIRREA defines the “appraisal management services” that an AMC provides to include appraisal review, they declined to expand on the issue in adopting the minimum standards.

**Alston & Bird Observation:** As AMCs and federally regulated financial institutions are aware, there is a distinction between the appraisal review requirements to which a state-registered AMC is subject (i.e., reviewing a certain percentage of all appraisals that are completed on its behalf, regardless of whether such appraisals were performed in connection with FRTs) and those to which a financial institution or its AMC agent is subject pursuant to Section 1110. Those who had hoped the minimum standards would provide some baseline for states to follow in consideration of the former are left disappointed.

### ***Implementation of the AMC National Registry fee requirement***

Although the number of appraisers on an AMC’s network or panel of appraisers will determine the size of the fee that each AMC must pay to the ASC’s AMC National Registry, the agencies note in the commentary to the final rule that the logistics of such fees are outside the scope of their rulemaking. Instead, implementation of the fee requirement will be left to the ASC. The minimum standards do provide, however, for states to report certain information on registered AMCs to the ASC and for federally regulated AMCs to provide information to the state(s) in which they operated to be included in such submissions.

**Alston & Bird Observation:** Whether the manner in which the AMC National Registry fee is implemented will impact the size of appraiser panels that AMCs maintain remains to be seen once the ASC engages in a separate rulemaking. For now, what is clear is that both state-registered AMCs and federally regulated AMCs will be subject to the requirement to pay such fees.

## **Conclusion**

While the minimum standards, compared to the proposed version of the rules, present very few surprises, they also leave a few important questions unanswered. We are hopeful that the agencies will be able to provide guidance on some of these, such as which entities will qualify as “federally regulated AMCs.” Furthermore, we are interested in how and when the agencies will engage in rulemaking to implement the appraisal review requirements of Section 1110 of FIRREA, and how the requirements of those rules will affect AMCs that may be subject to additional requirements under state laws. As states move forward with the process of implementing the minimum standards, Alston & Bird is available to assist clients with reviews of their compliance practices to ensure that they satisfy all laws applicable to AMCs.

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