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VIA Electronic Delivery

The Honorable Roberta A. Ouellette
Assistant Attorney General
Services to State Agencies Section
5830 Six Forks Road
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Re: North Carolina House Bill 829, An Act to Clarify the Definition of Customary and Reasonable Compensation for Real Estate Appraisers: Response to June 30, 2017 FTC Letter

Dear Assistant Attorney General Ouellette:

We respond on behalf of the North Carolina Real Estate Appraiser Association ("NCREAA") to the June 30, 2017 letter from the Federal Trade Commission's Acting Director of the Office of Policy Planning, Acting Director of the Bureau of Competition, and Director of the Bureau of Economics ("the FTC Letter") concerning House Bill 829 ("HB-829"). The NCREAA supports passage of HB-829, and would support further clarification of the bill to remove any threat of federal antitrust liability impeding the North Carolina Appraisal Board (the "Board") from fulfilling its obligation under the Dodd-Frank Act and state law to ensure the integrity of the residential appraisal process and, thereby, the housing market.

The FTC Letter raises two key questions. First, is HB-829 consistent with federal legislation regarding compensation for residential real estate appraisal services? The NCREAA believes that it is. The FTC Letter identifies a non-existent conflict between HB-829's provisions regarding the regulatory oversight of customary and reasonable ("C&R") fees to be paid by appraisal management companies ("AMCs") and the Dodd-Frank Act and its implementing regulations. Because North Carolina law requires the Board to register AMCs, the Dodd-Frank Act requires the Board to regulate C&R fees at or above the prescribed federal

minimum requirements, and allows states to adopt additional requirements to promote state policy interests. Second, would the actions of the Board pursuant to HB-829 qualify for "state action" immunity from federal antitrust liability, provided under Supreme Court precedents? The FTC Letter, by asking the question, acknowledges that such immunity could be available to the Board. Therefore, the NCREAA urges the North Carolina General Assembly to consider whether additional steps are necessary to secure antitrust immunity by establishing active supervision over the actions of the Board, and to require the Board to satisfy those requirements. In that regard, no active supervision is needed where a board is not controlled by active market participants.

In short, the Legislature has within its power to adopt HB-829's substantive provisions without violating Dodd-Frank mandates and to insulate the Board from potential conflict with the antitrust laws.

This letter provides additional background on the purpose of the Dodd-Frank Act and its requirements to regulate AMC payments for residential real estate appraisals, then addresses each of the above conclusions in turn.[1]

1. Dodd-Frank's Appraisal Independence and C&R Fee Provisions Protect Consumers as Mortgage Borrowers and Financial Institutions as Mortgage Holders. They Do Not Assure that AMCs Pay Low Fees for Residential Appraisals.

The Dodd-Frank Act's appraisal independence provisions, including its C&R fee requirement, protect consumers as borrowers with secured loans that are frequently in amounts of hundreds of thousands of dollars. Congress understood when enacting Dodd-Frank how flawed real estate appraisals contributed to the 2008-2009 financial crisis. Appraisers were pressured to place artificially high prices on properties: "Faulty appraisals can have real consequences: Individuals who obtained an overvalued appraisal may later encounter difficulty in refinancing or selling a home because the true value of the property used as collateral is less than the original mortgage."[2] And, AMCs sought out appraisers who would hit the desired price targets for a low appraisal fee: "Critics have also warned that the growth of AMCs may lead to a

[1] Constantine Cannon also is counsel to the Louisiana Real Estate Appraisers Board in connection with the FTC Louisiana Board Complaint referenced in the FTC Letter, which action was recently stayed for 90 days. (Order Granting in Part Motion to Stay Proceedings, *In the Matter of the Louisiana Real Estate Appraisers Board*, Dkt. No. 9374, July 28, 2017). Notwithstanding, all views expressed in this letter are solely the views of the NCREAA.

[2] H. Rep. 111-94 on H.R. 1728, at 56.

decline in appraisal quality. Because all appraisal fees are disclosed in a single line on closing documents, consumers and regulators currently lack the information needed to determine whether the growth of AMCs has led to low-cost, lower-quality appraisals."[3] As the Federal Reserve Board similarly observed when promulgating its interim rules: "According to some, appraisers willing to work for AMCs are often inexperienced in general or in the relevant geographic area and produce poor quality appraisals, undermining consumers' well-being and creditors' safety and soundness."[4]

The Dodd-Frank Act addressed these concerns through two relevant sections: (1) a new Appraisal Independence section of the Truth in Lending Act ("TILA") that established the C&R fee requirement for AMCs and lenders;[5] and (2) minimum requirements for state supervision of AMCs, including the requirement that AMCs must comply with new TILA Section 129E.[6] The legislative history of the Dodd-Frank Act and its implementing regulations demonstrates the goal to harmonize consumer protection and marketplace pricing objectives. Congress allowed AMC appraisal fees to reflect overall trends in appraisal pricing in particular geographies, subject to a requirement that all fees paid must be both customary and reasonable. This C&R requirement minimized financial incentives for AMCs to resume a race to the bottom by paying the lowest fee any appraiser is willing to accept, rather than a "customary and reasonable" fee for the specific services provided, the level of skill required, and the geographic market for the appraisal.

The FTC Letter (at page 4) expresses concern that the proposed North Carolina law would preclude AMCs from negotiating market-based fees with appraisers, and may ultimately result in "higher prices for consumers." The NCREAA believes this relies on an implicit assumption that "free-market" negotiation of transaction-specific appraisal fees would result in appraisers receiving a customary and reasonable fee. This assumption is wrong. The C&R requirement is a federally-mandated regulatory check on free market outcomes. However, if a negotiated fee is also customary and reasonable, HB-829 is no impediment.[7] What Dodd-Frank

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[3] *Id.*, at 59-60.

[4] 75 Fed. Reg. at 66570.

[5] Section 129E of TILA, 15 U.S.C. §1639e.

[6] Amending the 1989 Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA"), 12 U.S. C. § 3353.

[7] *See* 12 CFR Chapter X, Part 1026 Official Interpretation 42(f)(1)(5) ("Section 1026.42(f)(1) does not prohibit a fee appraiser and a creditor (or its agent) from agreeing to compensation based on transaction volume, so long as the compensation is customary and reasonable.").

and HB-829 properly do prevent is the ability of AMCs to drive down fees paid to residential appraisers to a point as low as any appraiser may be willing to go.

The history of the Dodd-Frank Act's amendments to TILA, and the Federal Reserve Board's implementing regulations demonstrate the fallacy of using the "free market" to determine transaction-specific appraisal fees. For example, TILA Section 129E specifically prohibits the use of fees paid by AMCs to residential appraisers as independent third-party evidence of what a C&R fee is: "Fee studies shall exclude assignments ordered by known appraisal management companies…."

The Federal Reserve Board's "Official Interpretations" for Section 129E (later adopted and re-codified by the Consumer Financial Protection Bureau) further rejects an agreement between appraisers and AMCs as a reliable indicator of whether an agreed "market-based" fee is customary and reasonable:

> *In theory*, the fact that an appraiser is willing to accept a particular fee for an appraisal assignment may bear on whether the fee is customary, reasonable, or both. However, an appraiser may be willing to accept a low fee because the appraiser is new to the industry and wishes to establish herself, or simply because the appraiser needs any work he can obtain in a slow housing market. In addition, the Board understands that some AMCs have begun requiring fee appraisers to agree that the fee is "customary and reasonable" as a condition of obtaining the appraisal assignment. In these situations, the Board believes that an appraiser's agreement that a fee is "customary and reasonable" *is an unreliable measure* of whether the fee in fact meets the statutory standard.

75 Fed. Reg. 66554 at 66571 (October 28, 2010) (emphasis added).[8]

The FTC Letter similarly contends (at page 4) that "to the extent that the legislative intent behind HB-829 is for the Board to require appraisal fees based on a survey, this approach also removes the free market from any role in determining the price of appraisal services." To the contrary, reliance on government price schedules or independent third-party studies is precisely the way Congress permitted the marketplace to influence the C&R fee determination. The only legislative presumption of compliance specified in Section 129E is: "Evidence for such [C&R] fees may be established by *objective third-party information, such as government agency fee schedules, academic studies, and independent private sector surveys*."[9] (Emphasis added.) And

[8] While the Federal Reserve Board acknowledged contrary views from AMC commenters on the nature and viability of the C&R fee requirement, the Interim Final Rules came down on the side of protecting the public policy interest in the integrity of federally-related real estate transactions by adopting the C&R rules discussed above. 75 Fed. Reg. at 66570.

[9] 15 U.S.C. §16393e(i)(b); (emphasis added).

the Federal Reserve Board specified that "customary" in customary and reasonable did not refer to fees in specific transactions, but only to fees paid over the course of time, generally a year, again reflecting the indirect manner in which market forces were to come into play. *See* 75 Fed. Reg. at 66569, 66586.

Moreover, there is no evidence that enforcement of a C&R requirement leads to higher prices paid by consumers or that a "free market" would lead to lower prices to consumers. In many appraisals, the lender pays a fixed fee to the AMC, regardless of the fees the AMC pays for an appraisal. The consumer similarly sees a single amount paid to the lender for the appraisal, combining whatever fee the AMC pays to the appraiser plus the amount the AMC charges the lender for its services. As a result, the amount the AMC pays to the appraiser affects only the AMC's margin on the transaction, not the price passed on to the consumer.

Finally, the FTC Letter observes (at page 5) "Congress specifically directed that Dodd-Frank was not intended to displace generally applicable antitrust principles, including the prohibition on unreasonable agreements in restraint of trade." However, nothing in the antitrust laws gives the Commission the ability to interpret regulations outside the scope of its jurisdiction contrary to the interpretations of the Federal Reserve Board and the Consumer Financial Protection Bureau, the agencies with such jurisdiction. And, nothing in the antitrust laws gives the Commission authority either to override a State's obligations under Dodd-Frank to protect the public interest by promoting the integrity and quality of residential mortgage appraisals (as set out in the next section), or to re-empower AMCs to compel appraisers to accept unduly low fees for inadequate appraisals.

2. The Dodd-Frank Act Compels the North Carolina Appraisal Board to Supervise the Fees Paid by AMCs to Appraisers to Ensure they are Customary and Reasonable to Protect the Integrity of the Appraisal Process.

Under Dodd-Frank section 1473 state appraiser licensing agencies are given enforcement authority only over AMC-ordered appraisals, not lender-ordered appraisals. The reason for this limitation was the emerging role of AMCs in the residential mortgage marketplace:

> According to some [2009] estimates, AMCs are now involved in more than 60 percent of appraisals and their market share is expected to grow…. AMCs, however, are subject to little direct oversight. Only in recent months have three States—Utah, Arkansas, and New Mexico—adopted laws requiring their registration and supervision.
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> In response to the growth of and concerns about AMCs, subsection [1473](f) creates a State-by-State system for registering and supervising AMCs … and it generally requires

> the system to be in place within 3 years of enactment. The subsection provides for the establishment of minimum standards to be applied in the registration of AMCs.[10]

More specifically, Dodd-Frank requires "minimum requirements to be established by a state in the registration of appraisal management companies."[11] That section further requires AMC oversight by a state's appraisal licensing agency, such as the Board. The minimum state requirements include that appraisals are conducted independently and free from inappropriate influence and coercion under the appraisal independence standard established under TILA section 129E.

Crucially, once a state registers AMCs—as North Carolina has pursuant to Article 2 of the North Carolina Appraisers Act—these minimum requirements become mandatory. As set out at 12 C.F.R § 34.213:

> Each State electing to register AMCs … must:
>
> (b) Impose requirements on AMCs that are not owned and controlled by an insured depository institution and not regulated by a Federal financial institutions regulatory agency to:
>
> (1) Register with and be subject to supervision by the State appraiser certifying and licensing agency;
>
> ***
>
> (5) Establish and comply with processes and controls reasonably designed to ensure that the AMC conducts its appraisal management services in accordance with the requirements of section 129E(a) through (i) of the Truth in Lending Act, 15 U.S.C. 1639e(a) through (i), and regulations thereunder.

The FTC Letter thus is incorrect when it states (at page 5), "neither the Final Rule nor Dodd-Frank requires the states to delegate enforcement of customary and reasonable fee requirements to active market participants." The statutory and regulatory mandate could not be clearer: AMCs must be registered and supervised by the State appraiser certifying and licensing agency. Since its establishment in 1993, the Board has been that agency for North Carolina.

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[10] H. Rep. 111-94 at 59-60, 97. Due to regulatory delays, the compliance deadline is now August 2018. 80 Fed. Reg. 32658, 32673.

[11] 12 USC § 3353(a).

Thus, as long as the Board certifies and licenses appraisers, it *must* register AMCs and enforce AMC compliance with the C&R requirement.

3. Dodd-Frank Authorizes States to Establish Requirements for AMCs that Go Beyond the Federal Minimums.

The FTC Letter (at page 3) suggests that the Federal Reserve Board rule "does not require states to impose upon AMCs standards for customary fees beyond what federal law provides…." While technically correct, the reverse is equally true: Nothing in the rule precludes states from exercising their own legislative judgment and regulatory authority to impose additional requirements on AMCs. Dodd-Frank makes clear that the mandatory minimums are just that—minimums: "Nothing in this section shall be construed to prevent States from establishing requirements in addition to any rules promulgated [by the federal financial regulatory agencies]."[12] Thus, to the extent that HB-829 does go beyond minimum federal requirements, the Legislature would be exercising North Carolina's sovereign right to go further to protect North Carolina consumers by ensuring the integrity of the mortgage appraisal process. In this context, for the Legislature to exercise its prerogative under 12 USC § 3353(b) to go beyond federal minimums would provide clarity as to how AMCs could demonstrate C&R rule compliance.

4. The Legislature Can Secure Immunity from Federal Antitrust Law for the Board's Implementation of HB-829 by Providing for Active Supervision of the Board's Activities Relating to the C&R Requirement.

Notwithstanding NCREAA's criticisms of the FTC Letter, as set out above, it agrees with the FTC Letter's ultimate observation that state regulatory boards do not inherently violate federal antitrust law by regulating price activity within their respective states. For example, no such liability might attach if the Board is not controlled by active market participants. *North Carolina State Bd. of Dental Examiners v. F.T.C.*, 135 S. Ct. 1101 (2015). And, even if a board is deemed to be controlled by active market participants, state action immunity would extend to a board where the state has clearly articulated an intent to displace competition and "where independent state officials actively supervise the Board's activities." FTC Letter at 5; *see N. C. Dental*, 135 S. Ct. at 1110. It therefore is within the Legislature's power, by amendment to HB-829, to ensure that the Board's regulatory and enforcement activities do not conflict with federal antitrust law.

[12] 12 USC § 3353(b). This preservation of states' rights also is included in the Final Rule at 12 C.F.R. § 34.210(d).

5. Conclusion

Contrary to the assertions of the FTC Letter, the Legislature would be acting in a manner consistent with Dodd-Frank and its implementing regulations if it were to enact HB-829 or similar legislation. Under the Dodd-Frank Act, North Carolina must establish a requirement that AMCs pay for appraisals for residential mortgages in an amount that is customary and reasonable in the relevant geographic area for the type of appraisal at issue. That requirement follows sound federal and state policies to protect North Carolina consumers as prospective mortgage borrowers. Any state requirements that exceed federal minimums for AMC regulation would be lawful Congressionally-anticipated exercises of North Carolina's sovereign ability to go beyond federal requirements as the Legislature deems appropriate to protect North Carolina consumers.

Further, the Legislature should consider appropriate amendments to HB-829 so that the Board may implement and enforce the AMC customary and reasonable fee requirements consistent with the requirements of federal antitrust law, such as under the doctrine of state action immunity as outlined in Section 4 above.

In sum, NCREAA supports the efforts of the Legislature to move forward with passage of HB-829 or similar legislation implementing the legislation's substantive provisions, and urges the Legislature to consider additional measures to assure the Board's ability to protect North Carolina consumers consistent with federal antitrust law.

Respectfully,

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