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To: Clients and Friends

From: David F. Dulock

Subject: Federal Reserve Board Interim Final Rule Adds Appraisal Independence Requirements - New Section 226.42 of Regulation Z

In the October 28, 2010, issue of the *Federal Register* (75 FR 66554), as corrected in the December 23, 2010, issue of the *Federal Register* (75 FR 80675), the Board of Governors of the Federal Reserve System (FRB) published an interim final rule (the Interim Rule) designed to ensure that real estate appraisers use their independent professional judgment in appraising homes without influence or pressure from parties interested in the loan transaction and that the appraiser receive customary and reasonable compensation for their services. The Interim Rule implements new Section 129E of the Truth in Lending Act (TILA), which was enacted as Section 1472 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Public Law 111-203) to establish new requirements for appraisal independence for consumer loans secured by the consumer's principal dwelling. To implement this new TILA appraisal independence requirement, the Interim Rule adds Section 226.42 to Regulation Z, which replaces Section 226.36(b) that contained similar appraisal requirements. Pursuant to the Dodd-Frank Act, *supra*, the issuance of this Interim Rule renders the Home Valuation Code of Conduct of no further force or effect. (*But see our October 18, 2010 memorandum on the new Fannie Mae Appraiser Independence Requirements in Fannie Mae Announcement SEL-2010-14.*)

Compliance with new Section 226.42 added by the Interim Rule is mandatory for all applications received by a creditor on or after April 1, 2011. The complete text of Section 226.42 is attached to this memorandum for your reference.

In order to assist you in understanding the Interim Rule's new appraisal independence requirements, this memorandum summarizes or redacts comments from the FRB's official staff interpretations of Section 226.42 and from the preamble published with the Interim Rule.

- **SECTION–BY-SECTION ANALYSIS – Section 226.42**

Subsection 42(a) Scope. The Interim Rule applies not only to a person who extends consumer credit secured by a consumer's principal dwelling, but also to any person who provides services in connection with a consumer credit transaction secured by a consumer's principal dwelling without regard to whether that person also extends consumer credit by originating mortgage loans. This means the Interim Rule applies to creditors, mortgage brokers, appraisal management companies, appraisers, real estate agents, title insurers, credit report providers, lawyers, document preparation providers, surveyors, pest inspectors, and other persons who provide settlement services as defined in the Real Estate Settlement Procedures Act (RESPA) and Regulation X. And, unlike the appraisal requirements of now removed Section 226.36(b), the Interim Rule's appraisal requirements apply to all consumer credit transactions secured by the consumer's principal dwelling (*i.e.*, closed-end loans as well as HELOCS).

Subsection 42(b) Definitions. The Interim Rule defines the following four terms for the purposes of appraisal independence under section 226.42:

(1) "Covered person" defines the persons who are subject to the prohibition on coercion and similar practices and the mandatory reporting requirement in the Interim Rule, and include a creditor with respect to a "covered transaction" or a person that provides settlement services as defined under RESPA and Regulation X with respect to a "covered transaction." (See *Scope* above for examples.)

(2) "Covered transaction" is a consumer credit transaction secured by the consumer's principal dwelling. The term 'principal dwelling" has the same meaning as it does in the definition of residential mortgage transaction in Section 226.2(a)(24), the right of rescission for open-end credit under Section 226.15(a) and the right of rescission for closed-end credit under Section 226.23(a) (*see* their respective comments 2(a)(24)-3, 15(a)(1)-5, and 23(a)(1)-3 in the official staff interpretations to Regulation Z).

(3) "Valuation" means an estimate of the value of the consumer's principal dwelling in written or electronic form (other than an estimate produced solely by an automated model or system). The Interim Rule uses the broad term "valuation," so that the prohibitions in Section 226.42 will apply to acts or practices that compromise the independent estimation of the value of the consumer's principal dwelling, without regard to whether the creditor uses a licensed or certified appraiser or another person to produce the valuation in question. The evaluation must be produced by a natural person (*e.g.*, appraisal report by an appraiser or a estimate of market value by a real estate agent) and includes photographic or other information included with the evaluation. The term includes an estimate of value provided or viewed electronically (*e.g.*, email or viewed using a computer). It also includes an estimate of a range of values for the consumer's principal dwelling and an estimate of value by a natural person based in part on an estimate produced by an automated system.

(4) "Valuation management functions" refers to the following administrative activities undertaken in connection with the preparation of a valuation. The term applies to a person that performs these administrative functions in connection with a valuation, even if the person is not an appraisal management company.

- Recruiting, selecting, or retaining a person to prepare a valuation.
- Contracting with or employing a person to prepare a valuation.
- Managing or overseeing the process of preparing a valuation (including by providing administrative services such as receiving an order for and receiving a valuation, submitting a completed valuation to a creditor or underwriter, collecting fees from a creditor or underwriter for services provided in connection with a valuation, and compensating a person that prepares a valuation); or
- Reviewing or verifying the work of a person that prepares a valuation.

Subsection 42(c) Valuation of Consumer's Principal Dwelling. Paragraph 42(c)(1) of this subsection of the Interim Rule prohibits a covered person from causing or attempting to cause the value assigned to the consumer's principal dwelling in connection with a covered transaction to be based on a factor other than the independent judgment of a person that prepares valuations,

through coercion, extortion, inducement, bribery or intimidation of, compensation or instruction to, or collusion with a person that prepares a valuation or a person that performs valuation management functions. These prohibited activities have the same meanings given them by applicable state law or contract. Subparagraph 42(c)(1)(i) provides examples (which are illustrative and not exhaustive) of prohibited acts and practices taken towards a person that prepares valuations, but paragraph 42(c)(1) also applies to prohibited acts and practices directed towards a person that performs valuation management functions or such person's affiliate. Further, although the examples assume a covered person's actions are designed to cause the value assigned to the consumer's principal dwelling to equal or exceed a certain amount, the Interim Rule also applies where a covered person's prohibited actions are designed to cause the value assigned to be below a certain amount. But, paragraph 42(c)(1) does not prohibit a covered person from requesting a person that prepares a valuation to take certain actions that does not replace the independent judgment of the person that prepares a valuation, such as requesting that the person who prepares a valuation (i) consider additional, appropriate property information, (ii) provide further information for the person's conclusion about the value, or (ii) correct errors in the valuation.

Paragraph 42(c)(2) prohibits mischaracterization of the appraised value of the consumer's principal dwelling securing a covered transaction through misrepresentation, falsification, alteration, or inducement. Subparagraph 42(c)(2)(i) provides that a person who prepares a valuation shall not materially misrepresent the value of the consumer's principal dwelling in a valuation. A *bona fide* error is not a misrepresentation because the intent is to prohibit intentional misrepresentations of value. Subparagraph 42(c)(2)(ii) provides that no covered person shall falsify, and no covered person other than a person who prepares the valuation shall materially alter, a valuation. A covered person may, however, request that a person who prepares a valuation take certain action permitted by Paragraph 42(c)(3), as for example, correcting errors in the valuation. Subparagraph 42(c)(2)(iii) provides that no covered person may induce a person to misrepresent the value in a valuation or falsify or materially alter a valuation. Note that subparagraph 42(c)(2)(i) applies specifically to persons that prepare valuations and subparagraphs 42(c)(2)(ii) and (iii) apply to all covered persons.

Paragraph 42(c)(3) provides six examples of actions that do not violate paragraphs 42(c)(1) [*coercion*] or 42(c)(2) [*mischaracterization of value*]. These examples are illustrative, not exhaustive, and there are other actions that are permitted under paragraphs 42(c)(1) or 42(c)(2). Subparagraph 42(c)(3)(i) provides that it is permissible to ask a person that prepares a valuation to consider additional property information, including information regarding comparable properties. Subparagraph 42(c)(3)(ii) provides that it is permissible to ask a person that prepares a valuation to provide further detail, substantiation, or explanation for the value conclusion. Subparagraph 42(c)(3)(iii) provides that it is permissible to ask a person that prepares a valuation to correct errors in the valuation. Subparagraph 42(c)(3)(iv) provides that it is permissible to obtain multiple valuations in order to select the most reliable valuation. Subparagraph 42(c)(3)(v) provides that it is permissible to withhold compensation for breach of contract or substandard performance of services. Subparagraph 42(c)(3)(vi) provides that it is permissible to take action permitted or required by applicable federal or state law or agency guidance.

<u>*Subsection 42(d) Prohibition on Conflicts of Interest*</u>. Subparagraph 42(d)(1)(i) prohibits a person preparing a valuation or performing valuation management functions for a consumer loan secured by the consumer's principal dwelling from having a direct or indirect interest, financial or otherwise, in the property or loan for which the valuation is or will be performed (called "a prohibited interest"). For example, a person preparing a valuation or performing valuation management functions has a prohibited interest if that person or an affiliate of that person also serves as a loan officer of the creditor, mortgage broker, real estate broker, or other settlement service provider for the loan, and the safe harbor conditions for settlement service providers in paragraph 42(d)(4) are not satisfied (*discussed below*). A person also has a prohibited interest if the person has any ownership or reasonably foreseeable ownership interest in the property (*e.g.*, purchaser-borrower) or is compensated or otherwise receives financial or other benefits based on whether the loan is consummated. Under the above examples (which are illustrative but not exhaustive) the person is not permitted to prepare the valuation or perform valuation management functions for the loan.

Subparagraph 42(d)(1)(ii)(A) provides that no person violates subparagraph 42(d)(1)(i) based solely on the fact that the person is an employee or affiliate of the creditor. In general, a creditor may use employees or affiliates to prepare a valuation or perform valuation management functions without violating subparagraph 42(d)(1)(i); but, whether an employee or affiliate has a direct or indirect interest in the property or transaction that creates a prohibited interest under subparagraph 42(d)(1)(i) depends on the facts and circumstances of a particular case, including the structure of the employment or affiliate relationship.

Similarly, subparagraph 42(d)(1)(ii)(B) provides that no person violates subparagraph 42(d)(1)(i) based solely on the fact that the person provides a settlement service in addition to preparing valuations or performing valuation management functions, or based solely on the fact that the person's affiliate performs another settlement service. In general, a person who prepares a valuation or performs valuation management functions may perform another settlement service for the same transaction without violating subparagraph 42(d)(1)(i), or the person's affiliate may provide another settlement service for the transaction; but, whether the person has a direct or indirect interest in the property or transaction that creates a prohibited interest under subparagraph 42(d)(1)(i) depends on the facts and circumstances of a particular case.

In order to reconcile the prohibition on conflicts of interest in subparagraph 42(d)(1)(i) with the exception in subparagraph 42(d)(1)(ii)(A), paragraphs 42(d)(2) and (d)(3) provide the following two safe harbors:

(1) Paragraph 42(d)(2) is for transactions in which the creditor had assets of more than $250 million as of December 31st for <u>both</u> of the past two calendar years; and
(2) Paragraph 42(d)(3) is for transactions in which the creditor had assets of $250 million or less as of December 31st for <u>either</u> of the past two calendar years.

Paragraph 42(d)(2) provides that, in a transaction in which the creditor had assets of more than $250 million as of December 31st for <u>both</u> of the past two calendar years, an employee or affiliate of the creditor who prepares a valuation or performs valuation management functions for that transaction does not have a conflict of interest in violation of subparagraph 42(d)(1)(i) based

on the person's employment or affiliate relationship with the creditor if:

(1) The compensation of the person is not based on the value arrived at in any valuation [for the transaction]; *(Note: The bracketed addition comes from the FRB preamble published with the Interim Rule.)*
(2) The person reports to a person who is not part of the creditor's loan production function and whose compensation is not based on the closing of the transaction to which the valuation relates; and
(3) No employee, officer or director in the creditor's loan production function is directly or indirectly involved in selecting, retaining, recommending or influencing the selection of the person to prepare a valuation or perform valuation management functions, or to be included in or excluded from a list of approved persons who prepare valuations or perform valuation management functions.

According to the FRB preamble published with the Interim Rule, condition (1) does not expressly prohibit basing the person's compensation on whether the transaction closes.

Comments from the official staff commentary interpreting condition (2) provide the following examples to clarify when condition (2) is not satisfied:

(1) If the person preparing a valuation or performing valuation management functions (i) is directly supervised or managed by a loan officer or other person in the creditor's loan production function, or (ii) by a person who is directly supervised or managed by a loan officer; or
(2) If the employee of an appraisal management company affiliated with the creditor for a transaction is in charge of valuation management for that transaction and is supervised by a person who earns a commission or bonus based on the percentage of closed transactions for which the appraisal management company provides valuation management functions.

Comments from the official staff commentary interpreting condition (3) provide the following example to clarify when condition (3) is not satisfied: if the person who selects the person who will prepare the valuation for a covered transaction is supervised by an employee of the creditor who also supervises loan officers.

Thus, paragraph 42(d)(2) provides a safe harbor for an employee or affiliate of the creditor if the conditions in (1), (2) and (3) above are satisfied. But, even if the above conditions are satisfied, the employee or affiliate who prepares a valuation or performs valuation management functions for that transaction may still have a prohibited conflict of interest under subparagraph 42(d)(1)(i) on other grounds – for example, if the employee or affiliate is the buyer or seller of the subject property in a purchase money mortgage transaction. If the conditions in (1), (2) and (3) above are not satisfied, however, whether the employee or affiliate has violated subparagraph 42(d)(1)(i) depends on all the facts and circumstances.

Paragraph 42(d)(3) provides that, in a transaction in which the creditor had assets of $250 million or less as of December 31st for <u>either</u> of the past two calendar years, an employee or

affiliate of the creditor who prepares a valuation or performs valuation management functions for that transaction does not have a conflict of interest in violation of subparagraph 42(d)(1)(i) based on the person's employment or affiliate relationship with the creditor if:

(1) The compensation of the person preparing a valuation or performing valuation management functions is not based the value arrived at in any valuation [for the transaction]; *(Note: The bracketed addition comes from the FRB preamble published with the Interim Rule, and as it parallels the same condition under paragraph 42(d)(2) discussed above, it also does not expressly prohibit basing the person's compensation on whether the transaction closes.)*; and
(2) The creditor requires that any employee, officer or director of the creditor who orders, performs, or reviews a valuation for a covered transaction (*see definition above*) abstain from participating in any decision to approve, not approve, or set the terms of that transaction.

Thus, paragraph 42(d)(3) provides a safe harbor for an employee or affiliate of the creditor if the conditions in (1) and (2) above are satisfied. But, even if the above conditions are satisfied, the employee or affiliate who prepares a valuation or performs valuation management functions for that transaction may still have a prohibited conflict of interest under subparagraph 42(d)(1)(i) on other grounds – for example, if the employee or affiliate is the buyer or seller of the subject property in a purchase money mortgage transaction. If the conditions in (1) and (2) above are not satisfied, however, whether the employee or affiliate has violated subparagraph 42(d)(1)(i) depends on all the facts and circumstances.

In order to reconcile the prohibition on conflicts of interest in subparagraph 42(d)(1)(i) with the exception in subparagraph 42(d)(1)(ii)(B), paragraph 42(d)(4) provides the following alternative safe harbors for persons who prepare valuations or perform valuation management functions for a covered transaction and provide other settlement service(s) for that transaction, or whose affiliate provides settlement service(s) for that transaction:

(1) Subparagraph 42(d)(4)(i) is for covered transactions in which the creditor had assets of more than $250 million as of December 31st for <u>both</u> of the past two calendar years; and
(2) Subparagraph 42(d)(4)(ii) is for covered transactions in which the creditor had assets of $250 million or less as of December 31st for <u>either</u> of the past two calendar years.

Under subparagraph 42(d)(4)(i), in a covered transaction in which the creditor had assets of more than $250 million for <u>both</u> of the past two calendar years, a person preparing a valuation or performing valuation management functions for that transaction in addition to performing another settlement service for that transaction, or whose affiliate performs another settlement service for that transaction, will not be deemed to have a prohibited interest under subparagraph 42(d)(1)(i) based on the fact that the person or the person's affiliate performs another settlement service for that transaction, as long as the three conditions in paragraph 42(d)(2) are met (*see conditions (1), (2) and (3) of paragraph 42(d)(2) discussed above*).

Likewise, under subparagraph 42(d)(4)(ii), in a covered transaction in which the creditor had assets of $250 million or less as of December 31st for <u>either</u> of the past two calendar years, a

person performing valuations or valuation management functions for that transaction in addition to performing another settlement service for that transaction, or whose affiliate performs another settlement service for that transaction, will not be deemed to have a prohibited interest under subparagraph 42(d)(1)(i) based on the fact that the person or the person's affiliate performs another settlement service for that transaction if the two conditions in paragraph 42(d)(3) are met (*see conditions (1) and (2) of paragraph 42(d)(3) discussed above*).

In general, the discussions regarding the safe harbors in paragraphs 42(d)(2) and 42(d)(3) are applicable to the safe harbors in subparagraphs 42(d)(4)(i) and (ii). But, there is a factual variation under subparagraph 42(d)(4)(i) – for example, assume an appraisal management company performs both valuation management functions and title services, including providing title insurance, for the covered transaction. If the title insurance agent in the transaction, whose compensation depends in whole or in part on whether title insurance is sold at the loan closing, supervises the appraisal management company employee in charge of valuation management functions for the transaction, the second condition in paragraph 42(d)(2) is not met.

Paragraph 42(d)(5) provides the following definitions for the purposes of subsection 42(d):

(1) "Loan production function" means an employee, officer, director, department, division, or other unit of a creditor responsible for generating covered transactions, approving covered transactions, or both. It includes, for example, retail sales staff, loan officers, and any other creditor employee responsible for taking a loan application, offering or negotiating loan terms or whose compensation is based on loan processing volume. It does not include, however, a person solely because part of the person's compensation includes a general bonus not tied to specific transactions or percentage of closed transactions, or a profit sharing plan that benefits all employees; nor does it include a person solely responsible for credit administration or risk management – for example, loan underwriting, loan closing functions (*e.g.*, loan documentation), disbursing funds, collecting mortgage payments and otherwise servicing the loan (*e.g.*, escrow management and payment of taxes), monitoring loan performance, and foreclosure processing.

(2) "Settlement service" has the same meaning as in RESPA. *See Section 3 of RESPA and Section 3500.2 of Regulation X for a detailed definition.*

(3) "Affiliate" has the same meaning as in Regulation Y (12 CFR 225.62(a)), which defines affiliate as any company that controls, is controlled by, or is under common control with, another company.

Subsection 42(e) When Extension of Credit Prohibited. In connection with a covered transaction, subsection 42(e) provides that a creditor who knows at or before loan consummation of a violation of subsection 42(c) or (d) - *i.e.*, coercion, mischaracterization of value and conflicts of interest, respectively - in connection with a valuation, must not extend credit based on that valuation, unless *the creditor documents that it has acted with reasonable diligence* to determine that the valuation does not materially misstate or misrepresent the value of the consumer's principal dwelling. Subsection 42(e) further provides that a valuation materially misstates or

misrepresents the value of the subject dwelling if the valuation contains a misstatement or misrepresentation affecting the credit decision or the credit terms.

Under subsection 42(e), a creditor acts with reasonable diligence if the creditor extends credit based on a valuation other than the suspect valuation; but, a creditor need not obtain a second valuation to document that the creditor acted with reasonable diligence to determine that the suspect valuation does not materially misstate or misrepresent the value of the subject dwelling. For example, assume that before loan closing an appraiser notifies the creditor that a covered person (*see definition in subsection 42(b) above*) tried, and failed, to get the appraiser to inflate the value of the subject dwelling. If the creditor reasonably determines and documents that the appraisal does not materially misstate or misrepresent the subject dwelling's value, the creditor may extend credit based on that appraisal.

Nothing in the Interim Rule mandates specific due diligence procedures for creditors to follow when they suspect a violation of subsection 42(c) or (d). Nor, under the Interim Rule, does a violation of subsection 42(e) establish a basis for voiding loan agreements (*i.e.*, even if a creditor knows of a violation of subsection 42(c) or (d) and nevertheless extends credit in violation of subsection 42(e), this violation does not itself void the consumer's loan agreement with the creditor). State or other applicable law determines whether the loan agreement is valid. Applicable federal or state laws or regulations, however, may require a creditor to take certain steps in the event the creditor knows about problems with a valuation.

Subsection 42(f) Customary and Reasonable Compensation. (**Please note that the requirements of subsection 42(f) only apply to compensation to fee appraisers and do not apply to compensation to non-fee appraisers.**) For a covered transaction, paragraph 42(f)(1) requires a creditor and its agent(s) to compensate a fee appraiser (*as defined in subparagraph 42(f)(4)(i) below*)) at a rate that is customary and reasonable for comparable appraisal services in the geographic market of the property being appraised. For the purposes of subsection 42(f):

(1) "agent" of the creditor is determined by applicable law, but a fee appraiser is not an agent of the creditor;
(2) "customary" fee means the fee must be reasonably related to recent rates for appraisal services in the geographic market of the property being appraised;
(3) "reasonable" fee means the fee be adjusted as necessary to account for factors, in addition to geographic market, that affect the level of compensation appropriate in a given transaction; and
(4) "geographic market of the property being appraised" means the geographic market relevant to compensation levels for appraisal services, which (depending on the facts and circumstances) could be a state, a metropolitan statistical area (MSA), a metropolitan division, an area outside of an MSA, a county or contagious counties, or other geographic area. The official staff commentary for paragraph 42(f)(1) provides two examples to illustrate this requirement:

> • [A]ssume that fee appraisers who normally work only in County A generally accept $400 to appraise an attached single-family property in County A. Assume also that *very few or no* fee appraisers who work only in contiguous County B will accept a rate comparable to $400 to appraise an attached single-family property in County A. The relevant geographic market for an attached single-family property in County A may reasonably be defined as County A.

> • [A]ssume that fee appraisers who normally work only in County A generally accept $400 to appraise an attached single-family property in County A. Assume also that *many* fee appraisers who normally work only in contiguous County B will accept a rate comparable to $400 to appraise an attached single-family property in County A. The relevant geographic market for an attached single-family property in County A may reasonably be defined to include both County A and County B.

Paragraph 42(f)(1) does not prohibit a creditor or its agent from withholding compensation from a fee appraiser for failing to meet contractual obligations (*e.g.*, failing to provide the appraisal report or violating state or federal appraisal laws in performing the appraisal).

Although paragraph 42(f)(1) is not intended to prohibit a creditor (or its agent) and a fee appraiser from negotiating a rate for an assignment in good faith or to prohibit a creditor (or its agent) from communicating to a fee appraiser the rates submitted by the other fee appraisers solicited for the assignment as part of this negotiation, a document signed by a fee appraiser indicating that the appraiser agrees that the fee paid to the appraiser is "customary and reasonable" does not by itself create a presumption of compliance with subsection 42(f) or otherwise satisfy the requirement to compensate the fee appraiser at a customary and reasonable rate. Objective factors or information such as that set forth in paragraphs 42(f)(2) and (f)(3) (*discussed below*) generally should support the determination by the creditor (or its agent) of the appropriate amount of compensation to pay a fee appraiser for a particular appraisal assignment.

Paragraph 42(f)(1) also is not intended to prevent a creditor (or its agent) and a fee appraiser from negotiating volume based discounts for a creditor that provides multiple appraisal assignments to a fee appraiser, so long as the compensation is customary and reasonable. The official staff commentary gives the following example of an acceptable volume based discount:

> [A]ssume that a fee appraiser typically receives $300 for appraisals from creditors with whom it does business; the fee appraiser, however, agrees to reduce the fee to $280 for a particular creditor, in exchange for a minimum number of assignments from the creditor.

Paragraphs 42(f)(2) and (f)(3) provide two alternative ways a creditor and its agent are presumed to comply with the compensation requirement in paragraph 42(f)(1):

(1) Under paragraph 42(f)(2), a creditor and its agent are presumed to compensate a fee appraiser in accordance with paragraph 42(f)(1) if:

• The amount of compensation is reasonably related to recent rates paid for comparable appraisal services performed in the geographic market of the property. In determining this amount, the creditor or its agent must identify recent rates and make any adjustments thereto necessary to account for (i) the type of property, (ii) the scope of work, (iii) the time in which the appraisal is required to be performed, and (iv) the fee appraiser's qualifications, experience, professional record and work quality; and

• The creditor and its agent do not engage in any anticompetitive actions in violation of state or federal law that affect the compensation paid to fee appraisers, such as (i) price-fixing or market allocation prohibited by relevant antitrust laws; or (ii) restricting any person from entering the relevant geographic market or causing any person to leave the relevant geographic market as prohibited by relevant antitrust laws.

(2) Under paragraph 42(f)(3), a creditor and its agent are also presumed to comply with the compensation requirement in paragraph 42(f)(1) if the creditor or its agent establishes the

compensation paid to the fee appraiser by relying on information about rates in the geographic market of the property being appraised that is based: (i) on objective third-party information, including fee schedules, studies, and surveys prepared by independent third parties such as government agencies, academic institutions, and private research firms (excluding compensation to fee appraisers for appraisals ordered by appraisal management companies); and, (ii) recent rates paid to a representative sample of fee appraisers or the fee schedules of those fee appraisers.

A creditor and its agent are presumed to comply with the requirement to pay a fee appraiser a customary and reasonable rate under paragraph 42(f)(1) if the creditor or its agent meets both conditions specified in paragraph 42(f)(2) above. These conditions are not requirements for compliance with paragraph 42(f)(1), but, if met, they create a presumption that the creditor or its agent has complied. Once a creditor or its agent has satisfied these conditions, a person may still rebut the presumption created thereby with evidence that the compensation paid to a fee appraiser was not customary and reasonable, which evidence must be unrelated to the conditions in paragraph 42(f)(2). Finally, if a creditor or its agent does not meet one of the conditions in paragraph 42(f)(2), compliance with the requirement to pay a fee appraiser at a customary and reasonable rate is determined based on all of the facts and circumstances without a presumption of either compliance or violation.

The first condition under paragraph 42(f)(2) requires the creditor or its agent to engage in a two-step process:

(i) Step one - the creditor or its agent must first identify the recent rates paid for comparable appraisal services in the relevant geographic market; and

(ii) Step two - once these rates have been identified, the creditor or its agent must then review the listed factors (*i.e.*, the type of property; the scope of work; the time in which the appraisal is required to be performed; and the fee appraiser's qualifications, experience, professional record and work quality) and make any appropriate adjustments to these rates to ensure that the fee appraiser's compensation is customary and reasonable for the particular appraisal assignment.

Under the step one, whether rates may reasonably be considered "recent" depends on the facts and circumstances, but generally a rate is considered "recent" if it has been charged within one year of the creditor's or its agent's reliance on this information to qualify for the presumption under paragraph 42(f)(2). To obtain information about "recent" rates, a creditor or its agent may use any reasonable method that provides information about rates for appraisal services in the relevant geographic market, such as using or performing a fee survey (although that is not required). The FRB preamble published with the Interim Rule states that qualifying for this presumption does not require that if third-party information is used that it exclude appraisals ordered by appraisal management companies (as is required to qualify for the presumption of compliance under subparagraph 42(f)(3)).

Under step two, since appraisal assignments vary and appraisers have different skills and experience, the factors listed above for this step, when applicable, must be taken into account in determining what level of compensation for a particular appraisal assignment is customary and reasonable. For example:

• If the recent rates identified by the creditor or its agent under step one were solely for appraisal assignments in which the scope of work required consideration of two comparable properties, but the current transaction requires an appraisal that considers three comparable properties, the creditor or its agent might reasonably adjust the rate by an amount that reasonably accounts for the increased scope of work.

• An appraisal requiring an interior inspection may be more expensive to perform and may warrant greater compensation than an appraisal requiring only an exterior inspection.

• An appraisal of a dwelling in a rural area with several additional outbuildings and significant acreage might be more expensive to perform and may warrant higher compensation for the appraiser than an appraisal of a detached single-family dwelling in a suburban area.

Because step two states that the rate must be adjusted as "necessary" in accordance with the listed factors to ensure a customary and reasonable rate of compensation, you should be aware that any one or more of these factors may not always be a factor (or be only a small factor) in determining what level of compensation is customary and reasonable for a particular appraisal assignment. For example, in a particular transaction, an appraiser with 20 years of experience may not necessarily provide a higher quality appraisal than an appraiser with five years of experience.

The below list of these factors contain examples of how they might apply to a particular transaction:

(1) *Type of property.* May include detached or attached single-family, condominium unit, cooperative unit, or manufactured home. The property type may contribute to the difficulty or ease of the appraisal assignment and, thus, can affect the value of the appraisal services.
(2) *Scope of work.* May include the type of inspection and the number of comparables required. The scope of work may vary based on a number of factors, such as the extent to which the property must be inspected, the type and extent of data that must be researched, and the type and extent of analyses required to reach credible conclusions. Thus, the compensation of an appraiser may reasonably be higher where the scope of work required for the appraisal is more extensive than the scope of work required for another appraisal performed by the same appraiser. (Note: To comply with the Uniform Standards of Professional Appraisal Practice (USPAP) - see subsection 42(g) below - appraisers must identify the extent of work and analysis required to obtain credible results for an appraisal assignment.)
(3) *Time in which to perform the appraisal services.* Sometime called "turnaround" time. In the Interim Rule preamble, the FRB states that while it recognizes that required turnaround time can be a legitimate factor to consider in determining the appraiser's rate, appraiser competency and an accurate appraisal should be the creditor's chief concerns, and that the FRB expects creditors and their agents to select an appraiser foremost on the basis of the appraiser's education, expertise and competence to complete the assignment.
(4) *Fee appraiser qualifications.* Professional qualifications that appropriately affect the value of appraisal services include whether the appraiser is state licensed or state certified in accordance with the minimum criteria issued by the Appraisal Qualifications Board of

the Appraisal Foundation - for example, a state licensed appraiser could legitimately command a higher rate for appraisal services than an appraiser-in training who has not yet received a license. Relevant qualifications may also include the appraiser's completion of continuing education courses on effective appraisal methods and related topics. But, permitting a creditor to consider an appraiser's qualifications does not override state or federal laws prohibiting the exclusion of an appraiser from consideration for an assignment solely because of membership or lack of membership in any particular appraisal organization.

(5) *Fee appraiser experience and professional record.* The fee appraiser's level of experience may include the fee appraiser's years of service as a state licensed or state certified appraiser, or years of service appraising properties in a particular geographical area or of a particular type. The FRB preamble states that a fee for appraisal services may reasonably be higher when the fee appraiser has been state licensed or state certified for a number of years (*e.g.*, 15 years) and has been appraising properties in the relevant geographic area during all that time than when the fee appraiser is more recently licensed and has appraised properties in that area for only months (*e.g.*, six months). The fee appraiser's professional record may include whether the fee appraiser has a past record of suspensions, disqualifications, debarments, or judgments for waste, fraud, abuse or breach of legal or professional standards. The FRB preamble states that a creditor or its agent should exercise caution in engaging a fee appraiser with a blemished professional record, and should carefully scrutinize the appraiser's work, and that a creditor or its agent might reasonably pay less for that fee appraiser's services than for the services of a fee appraiser with an unblemished record.

(6) *Fee appraiser work quality.* Principally comprises the soundness of the appraiser's appraisal assignments. It may include the past quality of appraisals performed by the appraiser based on the written performance and review criteria of the creditor or its agent. A creditor or its agent might reasonably pay a fee appraiser with an excellent performance history at a higher rate than a fee appraiser with a performance history showing problems with past assignments.

The second condition under subparagraph 42(f)(2), which requires the creditor and its agent to not engage in any anticompetitive acts in violation of state or federal law that affect the compensation of fee appraisers - such as price fixing, market allocation or monopolization - must also be complied with in order to qualify for the presumption of compliance under paragraph 42(f)(2), notwithstanding that the creditor or its agent has satisfied the first condition under paragraph 42(f)(2) discussed above. The official staff commentary provides several examples of these prohibited anticompetitive acts:

• *Price fixing-*

> If appraisal management company A and appraisal management company B agreed to compensate fee appraisers at no more than a specific rate or range of rates, neither appraisal management company would qualify for the presumption of compliance.

• *Market allocation-*

> [I]f appraisal management company A and appraisal management company B agreed that appraisal management company A would limit its business to a certain portion of the relevant geographic market and appraisal management company B would limit its business to a different portion of the relevant

> geographic market, and as a result each appraisal management company unilaterally set the fees paid to fee appraisers in their respective portions of the market, neither appraisal management company would qualify for the presumption of compliance under paragraph (f)(2).

• *Monopolization-*

> [I]f only one appraisal management company exists or is predominant in a particular market area, that appraisal management company might not qualify for the presumption of compliance if it entered into exclusivity agreements with all creditors in the market or all fee appraisers in the market, such that other appraisal management companies had to leave or could not enter the market. Whether this behavior would be considered an anticompetitive act that affects the compensation paid to fee appraisers depends on all of the facts and circumstances, including applicable law.

As stated above, in addition to the presumption of compliance described in paragraph 42(f)(2), paragraph 42(f)(3) provides creditors and their agents with an alternative means to qualify for a presumption of compliance with the requirement to pay fee appraisers at a customary and reasonable rate under paragraph 42(f)(1); but only if the creditor or its agent satisfies the three conditions specified in paragraph 42(f)(3). (*Please refer back to paragraph 42(f)(3) for a description of those conditions.*) For the purposes of paragraph 42(f)(3):

(1) "geographic market" has the same meaning as discussed above under paragraph 42 (f)(1) – *i.e.*, the geographic market relevant to compensation levels for appraisal services, which (depending on the facts and circumstances) could be a state, a metropolitan statistical area (MSA), a metropolitan division, an area outside of an MSA, a county or contagious counties, or other geographic area; and
(2) "recent" rates depends on the facts and circumstances, but generally would include rates charged within one year of the creditor's or its agent's reliance on this information to qualify for the presumption of compliance under paragraph 42(f)(3).

A creditor and its agent are presumed to comply with the requirement to pay a fee appraiser a customary and reasonable rate under paragraph 42(f)(1) if the creditor or its agent determine the rate based on information that satisfies the conditions specified in paragraph 42(f)(3). Relying on information that satisfies these conditions is not a requirement for compliance with paragraph 42(f)(1), but creates a presumption that the creditor or its agent has complied. Once a creditor or its agent has satisfied these conditions, a person may still rebut the presumption created thereby with evidence that the compensation paid to a fee appraiser was not customary and reasonable, which evidence must be unrelated to the information that satisfies the conditions in paragraph 42(f)(3). Finally, if a creditor or its agent does not rely on information that satisfies the conditions in paragraph 42(f)(3), compliance with the paragraph 42(f)(1) requirement to pay a fee appraiser at a customary and reasonable rate is determined based on all of the facts and circumstances without a presumption of either compliance or violation.

Lastly, paragraph 42(f)(4) defines the following three terms for purposes of customary and reasonable compensation under subsection 42(f):

(1) "Fee appraiser" means (i) a natural person who is a state licensed or state certified appraiser and receives a fee for performing an appraisal, but who is not an employee of the person engaging the appraiser; or (ii) an organization that, in the ordinary course of business, employs state licensed or state certified appraisers to perform appraisals, receives a fee for performing

appraisals, and is not subject to the requirements of section 1124 of FIRREA (12 U.S.C. 3331 *et seq.*). Note: *The FRB preamble to the Interim Rule states that section 1124, as added by the Dodd-Frank Act, requires the federal banking agencies and the FHFA to issue rules that require an appraisal management company (as defined by FIRREA) to register with state appraiser certifying and licensing agencies according to minimum criteria set by these rules. Thus, only organizations that perform appraisals and that would not be required to register under these new rules satisfy the fee appraiser definition in paragraph 42(f)(4).*

(2) "Appraisal services" means only the services required to perform the appraisal, including defining the scope of work, inspecting the property, reviewing necessary and appropriate public and private data sources (for example, multiple listing services, tax assessment records and public land records), developing and rendering an opinion of value, and preparing and submitting the appraisal report. *Note: The FRB preamble states that because an appraisal management company (AMC), as agent of the creditor, splits the total appraisal fee between the AMC (for appraisal management functions) and the appraiser (for the appraisal), this definition is intended to clarify that the customary and reasonable rate paid to the fee appraiser (see paragraph 42(f)(1)) applies only to compensation for tasks that the fee appraiser performs (appraisal services), not the entire cost of the appraisal (including management functions).*

(3) "Appraisal management company" means as any person authorized to do one or more of the following actions on behalf of the creditor: (i) recruit, select, and retain fee appraisers; (ii) contract with fee appraisers to perform appraisal services; (iii) manage the process of having an appraisal performed, including providing administrative duties such as receiving appraisal orders and appraisal reports, submitting completed appraisal reports to creditors and underwriters, collecting fees from creditors and underwriters for services provided, and compensating fee appraisers for services performed; or (iv) review and verify the work of fee appraisers.

Subsection 42(g) Mandatory Reporting. (**Please note that the reporting requirements of subsection 42(g) only apply to activities by appraisers and do not apply to activities by non-appraisers who provide valuations.**) Paragraph 42(g)(1) requires a covered person who reasonably believes that an appraiser has materially failed to comply with (i) the Uniform Standards of Professional Appraisal Practice (USPAP) or (ii) an ethical or professional requirement for appraisers under applicable state or federal statutes or regulations, to report said failure to the appropriate state agency. For the purposes of paragraph 42(g)(1):

(1) A "covered person" includes creditors, mortgage brokers, appraisers, appraisal management companies, real estate agents, and other persons that provide "settlement services" as defined under RESPA and Regulation X implementing RESPA; and,
(2) An "appraiser" is a natural person who provides opinions of the value of dwellings and is required to be licensed or certified under the laws of the state in which the consumer's principal dwelling is located or otherwise is subject to the jurisdiction of the appraiser certifying and licensing agency for that state.

Under paragraph 42(g)(1), a covered person reasonably believes that an appraiser has materially failed to comply with USPAP or the applicable ethical or professional statutory or regulatory requirements if the person has knowledge or information that would lead a reasonable person in the same circumstances to conclude that the appraiser has materially failed to comply

with USPAP or such statutory or regulatory requirements.

Paragraph 42(g)(1) defines a material failure to comply as a failure that is likely to significantly affect the value assigned to the consumer's principal dwelling - for example: (1) materially misrepresenting the value of the consumer's principal dwelling, in violation of subparagraph 42(c)(2)(i); (2) performing an appraisal in a grossly negligent manner, in violation of USPAP; or (3) accepting an appraisal assignment on the condition that the appraiser will report a value equal to or greater than the purchase price for the consumer's principal dwelling, in violation of USPAP. These examples are illustrative and not exhaustive of a material failure to comply under paragraph 42(g)(1).

Paragraph 42(g)(1) does not require reporting non-material failures to comply - for example, an appraiser's disclosure of confidential information in violation of applicable state law or an appraiser's failure to maintain errors and omissions insurance in violation of applicable state law are not material failures for purposes of paragraph 42(g)(1).

Paragraph 42(g)(2) provides that a covered person must report a material failure to comply to the appropriate state agency within a reasonable period of time after the person determines that there is a reasonable basis to believe that such a material failure to comply has occurred. However, neither paragraph 42(g)(2) nor its official staff interpretations establish or provide guidance on what constitutes a reasonable period of time by which a person must report a failure to comply with USPAP or ethical or professional requirements.

Paragraph 42(g)(3) defines the term "state agency" to mean the "state appraiser certifying and licensing agency" defined by Title XI of FIRREA (12 U.S.C. 3350(1)) and any implementing regulations. Paragraph 42(g)(3) clarifies that the state appraiser certifying and licensing agency for the state in which the consumer's principal dwelling is located is the appropriate state agency to which to report a material failure to comply.

- **MANDATORY DATE**

Compliance with the Interim Rule is mandatory for all consumer credit loans (*i.e.*, open-end and closed-end) secured by the consumer's principal dwelling for which a creditor receives an application on or after April 1, 2011.

- **CONCLUSION**

We advise you not to rely exclusively on this memorandum in understanding and applying the the Interim Rule, but to read the text of and the explanatory preamble to the Interim Rule, which may be accessed at: http://edocket.access.gpo.gov/2010/pdf/2010-26671.pdf, as corrected by the FRB at: http://www.gpo.gov/fdsys/pkg/FR-2010-12-23/pdf/2010-31824.pdf.

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PART 226—TRUTH IN LENDING (REGULATION Z)
Subpart E—Special Rules for Certain Home Mortgage Transactions

§ 226.42 Valuation independence.

(a) ***Scope***. This section applies to any consumer credit transaction secured by the consumer's principal dwelling.

(b) ***Definitions***. For purposes of this section:

(1) "Covered person" means a creditor with respect to a covered transaction or a person that provides "settlement services," as defined in 12 U.S.C. 2602(3) and implementing regulations, in connection with a covered transaction.

(2) "Covered transaction" means an extension of consumer credit that is or will be secured by the consumer's principal dwelling, as defined in §226.2(a)(19).

(3) "Valuation" means an estimate of the value of the consumer's principal dwelling in written or electronic form, other than one produced solely by an automated model or system.

(4) "Valuation management functions" means:

(i) Recruiting, selecting, or retaining a person to prepare a valuation;

(ii) Contracting with or employing a person to prepare a valuation;

(iii) Managing or overseeing the process of preparing a valuation, including by providing administrative services such as receiving orders for and receiving a valuation, submitting a completed valuation to creditors and underwriters, collecting fees from creditors and underwriters for services provided in connection with a valuation, and compensating a person that prepares valuations; or

(iv) Reviewing or verifying the work of a person that prepares valuations.

(c) ***Valuation of consumer's principal dwelling*** —(1) *Coercion.* In connection with a covered transaction, no covered person shall or shall attempt to directly or indirectly cause the value assigned to the consumer's principal dwelling to be based on any factor other than the independent judgment of a person that prepares valuations, through coercion, extortion, inducement, bribery, or intimidation of, compensation or instruction to, or collusion with a person that prepares valuations or performs valuation management functions.

(i) Examples of actions that violate paragraph (c)(1) include:

(A) Seeking to influence a person that prepares a valuation to report a minimum or maximum value for the consumer's principal dwelling;

(B) Withholding or threatening to withhold timely payment to a person that prepares a valuation or performs valuation management functions because the person does not value the consumer's principal dwelling at or above a certain amount;

(C) Implying to a person that prepares valuations that current or future retention of the person depends on the amount at which the person estimates the value of the consumer's principal dwelling;

(D) Excluding a person that prepares a valuation from consideration for future engagement because the person reports a value for the consumer's principal dwelling that does not meet or exceed a predetermined threshold; and

(E) Conditioning the compensation paid to a person that prepares a valuation on consummation of the covered transaction.

(2) *Mischaracterization of value* —(i) *Misrepresentation.* In connection with a covered transaction, no person that prepares valuations shall materially misrepresent the value of the consumer's principal dwelling in a valuation. A misrepresentation is material for purposes of this paragraph (c)(2)(i) if it is likely to significantly affect the value assigned to the consumer's principal dwelling. A *bona fide* error shall not be a misrepresentation.

(ii) *Falsification or alteration.* In connection with a covered transaction, no covered person shall falsify and no covered person other than a person that prepares valuations shall materially alter a valuation. An alteration is material for purposes of this paragraph (c)(2)(ii) if it is likely to significantly affect the value assigned to the consumer's principal dwelling.

(iii) *Inducement of mischaracterization.* In connection with a covered transaction, no covered person shall induce a person to violate paragraph (c)(2)(i) or (ii) of this section.

(3) *Permitted actions.* Examples of actions that do not violate paragraph (c)(1) or (c)(2) include:

(i) Asking a person that prepares a valuation to consider additional, appropriate property information, including information about comparable properties, to make or support a valuation;

(ii) Requesting that a person that prepares a valuation provide further detail, substantiation, or explanation for the person's conclusion about the value of the consumer's principal dwelling;

(iii) Asking a person that prepares a valuation to correct errors in the valuation;

(iv) Obtaining multiple valuations for the consumer's principal dwelling to select the most reliable valuation;

(v) Withholding compensation due to breach of contract or substandard performance of services; and

(vi) Taking action permitted or required by applicable federal or state statute, regulation, or agency guidance.

(d) *Prohibition on conflicts of interest* —(1)(i) *In general.* No person preparing a valuation or performing valuation management functions for a covered transaction may have a direct or indirect interest, financial or otherwise, in the property or transaction for which the valuation is or will be performed.

(ii) *Employees and affiliates of creditors; providers of multiple settlement services.* In any covered transaction, no person violates paragraph (d)(1)(i) of this section based solely on the fact that the person—

(A) Is an employee or affiliate of the creditor; or

(B) Provides a settlement service in addition to preparing valuations or performing valuation management functions, or based solely on the fact that the person's affiliate performs another settlement service.

(2) *Employees and affiliates of creditors with assets of more than $250 million for both of the past two calendar years.* For any covered transaction in which the creditor had assets of more than $250 million as of December 31st for both of the past two calendar years, a person subject to paragraph (d)(1)(i) of this section who is employed by or affiliated with the creditor does not have a conflict of interest in violation of paragraph (d)(1)(i) of this section based on the person's employment or affiliate relationship with the creditor if:

(i) The compensation of the person preparing a valuation or performing valuation management functions is not based on the value arrived at in any valuation;

(ii) The person preparing a valuation or performing valuation management functions reports to a person who is not part of the creditor's loan production function, as defined in paragraph (d)(5)(i) of this section, and whose compensation is not based on the closing of the transaction to which the valuation relates; and

(iii) No employee, officer or director in the creditor's loan production function, as defined in paragraph (d)(5)(i) of this section, is directly or indirectly involved in selecting, retaining, recommending or influencing the selection of the person to prepare a valuation or perform valuation management functions, or to be included in or excluded from a list of approved persons who prepare valuations or perform valuation management functions.

(3) *Employees and affiliates of creditors with assets of $250 million or less for either of the past two calendar years.* For any covered transaction in which the creditor had assets of $250 million or less as of December 31st for either of the past two calendar years, a person subject to paragraph (d)(1)(i) of this section who is employed by or affiliated with the creditor does not have a conflict of interest in violation of paragraph (d)(1)(i) of this section based on the person's employment or affiliate relationship with the creditor if:

(i) The compensation of the person preparing a valuation or performing valuation management functions is not based on the value arrived at in any valuation; and

(ii) The creditor requires that any employee, officer or director of the creditor who orders, performs, or reviews a valuation for a covered transaction abstain from participating in any decision to approve, not approve, or set the terms of that transaction.

(4) *Providers of multiple settlement services.* For any covered transaction, a person who prepares a valuation or performs valuation management functions in addition to performing another settlement service for the transaction, or whose affiliate performs another settlement service for the transaction, does not have a conflict of interest in violation of paragraph (d)(1)(i) of this section as a result of the person or the person's affiliate performing another settlement service for the transaction if:

(i) The creditor had assets of more than $250 million as of December 31st for both of the past two calendar years and the conditions in paragraph (d)(2)(i)–(iii) are met; or

(ii) The creditor had assets of $250 million or less as of December 31st for either of the past two calendar years and the conditions in paragraph (d)(3)(i)–(ii) are met.

(5) *Definitions.* For purposes of this paragraph, the following definitions apply:

(i) *Loan production function.* The term “loan production function” means an employee, officer, director, department, division, or other unit of a creditor with responsibility for generating covered transactions, approving covered transactions, or both.

(ii) *Settlement service.* The term “settlement service” has the same meaning as in the Real Estate Settlement Procedures Act, 12 U.S.C. 2601 *et seq.*

(iii) *Affiliate.* The term “affiliate” has the same meaning as in Regulation Y, 12 CFR 225.2(a).

(e) *When extension of credit prohibited*. In connection with a covered transaction, a creditor that knows, at or before consummation, of a violation of paragraph (c) or (d) of this section in connection with a valuation shall not extend credit based on the valuation, unless the creditor documents that it has acted with reasonable diligence to determine that the valuation does not materially misstate or misrepresent the value of the consumer's principal dwelling. For purposes of this paragraph (e), a valuation materially misstates or misrepresents the value of the consumer's principal dwelling if the valuation contains a misstatement or misrepresentation that affects the credit decision or the terms on which credit is extended.

(f) *Customary and reasonable compensation* —(1) *Requirement to provide customary and reasonable compensation to fee appraisers.* In any covered transaction, the creditor and its agents shall compensate a fee appraiser for performing appraisal services at a rate that is customary and reasonable for comparable appraisal services performed in the geographic market of the property being appraised. For purposes of paragraph (f) of this section, “agents” of the creditor do not include any fee appraiser as defined in paragraph (f)(4)(i) of this section.

(2) *Presumption of compliance.* A creditor and its agents shall be presumed to comply with paragraph (f)(1) if—

(i) The creditor or its agents compensate the fee appraiser in an amount that is reasonably related to recent rates paid for comparable appraisal services performed in the geographic market of the property being appraised. In determining this amount, a creditor or its agents shall review the factors below and make any adjustments to recent rates paid in the relevant geographic market necessary to ensure that the amount of compensation is reasonable:

(A) The type of property,

(B) The scope of work,

(C) The time in which the appraisal services are required to be performed,

(D) Fee appraiser qualifications,

(E) Fee appraiser experience and professional record, and

(F) Fee appraiser work quality; and

(ii) The creditor and its agents do not engage in any anticompetitive acts in violation of state or federal law that affect the compensation paid to fee appraisers, including—

(A) Entering into any contracts or engaging in any conspiracies to restrain trade through methods such as price fixing or market allocation, as prohibited under section 1 of the Sherman Antitrust Act, 15 U.S.C. 1, or any other relevant antitrust laws; or

(B) Engaging in any acts of monopolization such as restricting any person from entering the relevant geographic market or causing any person to leave the relevant geographic market, as prohibited under section 2 of the Sherman Antitrust Act, 15 U.S.C. 2, or any other relevant antitrust laws.

(3) *Alternative presumption of compliance.* A creditor and its agents shall be presumed to comply with paragraph (f)(1) if the creditor or its agents determine the amount of compensation paid to the fee appraiser by relying on information about rates that:

(i) Is based on objective third-party information, including fee schedules, studies, and surveys prepared by independent third parties such as government agencies, academic institutions, and private research firms;

(ii) Is based on recent rates paid to a representative sample of providers of appraisal services in the geographic market of the property being appraised or the fee schedules of those providers; and

(iii) In the case of information based on fee schedules, studies, and surveys, such fee schedules, studies, or surveys, or the information derived therefrom, excludes compensation paid to fee appraisers for appraisals ordered by appraisal management companies, as defined in paragraph (f)(4)(iii) of this section.

(4) *Definitions.* For purposes of this paragraph (f), the following definitions apply:

(i) *Fee appraiser.* The term “fee appraiser” means—

(A) A natural person who is a state-licensed or state-certified appraiser and receives a fee for performing an appraisal, but who is not an employee of the person engaging the appraiser; or

(B) An organization that, in the ordinary course of business, employs state-licensed or state-certified appraisers to perform appraisals, receives a fee for performing appraisals, and is not subject to the requirements of section 1124 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (12 U.S.C. 3331 *et seq.*).

(ii) *Appraisal services.* The term “appraisal services” means the services required to perform an appraisal, including defining the scope of work, inspecting the property, reviewing necessary and appropriate public and private data sources (for example, multiple listing services, tax assessment records and public land records), developing and rendering an opinion of value, and preparing and submitting the appraisal report.

(iii) *Appraisal management company.* The term “appraisal management company” means any person authorized to perform one or more of the following actions on behalf of the creditor—

(A) Recruit, select, and retain fee appraisers;

(B) Contract with fee appraisers to perform appraisal services;

(C) Manage 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 underwriters, collecting fees from creditors and underwriters for services provided, and compensating fee appraisers for services performed; or

(D) Review and verify the work of fee appraisers.

(g) ***Mandatory reporting*** —(1) *Reporting required.* Any covered person that reasonably believes an appraiser has not complied with the Uniform Standards of Professional Appraisal Practice or ethical or professional requirements for appraisers under applicable state or federal statutes or regulations shall refer the matter to the appropriate state agency if the failure to comply is material. For purposes of this paragraph (g)(1), a failure to comply is material if it is likely to significantly affect the value assigned to the consumer's principal dwelling.

(2) *Timing of reporting.* A covered person shall notify the appropriate state agency within a reasonable period of time after the person determines that there is a reasonable basis to believe that a failure to comply required to be reported under paragraph (g)(1) of this section has occurred.

(3) *Definition.* For purposes of this paragraph (g), “state agency” means “state appraiser certifying and licensing agency” under 12 U.S.C. 3350(1) and any implementing regulations. The appropriate state agency to which a covered person must refer a matter under paragraph (g)(1) of this section is the agency for the state in which the consumer's principal dwelling is located.