Public Interest Comment\(^1\) on

The Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corporation, Bureau of Consumer Financial Protection, Federal Housing Finance Agency’s Proposed Rule:

Minimum Requirements for Appraisal Management Companies

Docket ID No. CFPB 2014-0006
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The George Washington University Regulatory Studies Center

Retrospective Review Comment Project

The George Washington University Regulatory Studies Center works to improve regulatory policy through research, education, and outreach. As part of its mission, the Center conducts careful and independent analyses to assess rulemaking proposals from the perspective of the public interest. This comment on the Department of Treasury, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, Bureau of Consumer Financial Protection, and Federal Housing Finance Agency’s (collectively, ‘the Agencies’) jointly proposed rule, inter alia, to implement the Minimum Requirements applied by States in the registration and supervision of appraisal management companies (AMCs) does not represent the views of any particular affected party or special interest, but is designed to evaluate whether the Agencies’ proposal incorporates plans for retrospective review, pursuant to Executive Orders 13563 and 13579.

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\(^1\) This comment reflects the views of the author, and does not represent an official position of the GW Regulatory Studies Center or the George Washington University. The Center’s policy on research integrity is available at [http://regulatorystudies.columbian.gwu.edu/policy-research-integrity](http://regulatorystudies.columbian.gwu.edu/policy-research-integrity).

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Introduction

In this NPRM, the Agencies jointly propose to implement the minimum requirements (‘Minimum Requirements’) in the Dodd-Frank Act to be applied by states in the registration and supervision of appraisal management companies (AMCs). While the Act does not require states to establish a compliant AMC registration and supervision program, AMCs can no longer engage in “federally-related transactions,” such as real estate-related financial transactions overseen by a federal financial institution regulatory agency, in states that have not. Minimum Requirements are imposed on AMCs that do register and become licensed. Licensed AMCs must only use state-certified, independently chosen appraisers.

State licensing agencies must have the power to: approve and deny initial and renewal applications from AMCs; to examine the books and records of AMCs; to require AMCs to submit relevant information to the state; to verify that appraisers hold valid state licenses; and to discipline AMCs that violate the rules.

The proposed rule also implements the requirement in the Dodd-Frank Act for states to report certain activities of AMCs to the Appraisal Subcommittee (ASC), which administers the AMC National Registry of the Federal Financial Institutions Examination Council (FFIEC).

The rule primarily affects participating states, AMCs, appraisers, banks involved in mortgage financing and homebuyers.

As a part of its ongoing Retrospective Review Comment Project, the GW Regulatory Studies Center examines significant proposed regulations to assess whether agencies propose retrospective review as a part of their regulations, and submits comments to provide suggestions on how best to incorporate plans for retrospective review into their proposals. To facilitate meaningful retrospective review after the promulgation of a final rule, multiple government guidelines instruct agencies to incorporate retrospective review plans into their proposals during the rulemaking process.

Incorporating Retrospective Review into NPRMs

Through a series of Executive Orders, President Obama has encouraged federal regulatory agencies to review existing regulations “that may be outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned.” On January 18, 2011, President Obama signed Executive Order 13563, Improving Regulation and Regulatory Review, which reaffirmed the regulatory principles and structures outlined in EO 12866. In addition to the regulatory philosophy laid out in EO 12866, EO 13563 instructs agencies to
consider how best to promote retrospective analysis of rules that may be outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned. Such retrospective analyses, including supporting data, should be released online whenever possible.³

This ex-post review makes it possible for the public—and for the agencies that regulate them—to measure whether a particular rule has had its intended effect. In his implementing memo on retrospective review, former Administrator of the Office of Information and Regulatory Affairs, Cass Sunstein, stated the importance of designing regulations to facilitate their evaluation:

> With its emphasis on “periodic review of existing significant regulations,” Executive Order 13563 recognizes the importance of maintaining a consistent culture of retrospective review and analysis throughout the executive branch. To promote that culture, *future regulations should be designed and written in ways that facilitate evaluation of their consequences* and thus promote retrospective analyses and measurement of “actual results.” To the extent permitted by law, agencies should therefore give careful consideration to how best to promote empirical testing of the effects of rules both in advance and retrospectively.⁴

[Emphasis added]

This emphasis is repeated in Sunstein’s June 14, 2011 memo, “Final Plans for Retrospective Analysis of Existing Rules.” In its Draft 2013 Report to Congress on the Benefits and Costs of Federal Regulations, the Office of Management and Budget (OMB) states that such retrospective analysis can serve as an important corrective mechanism to the flaws of ex ante analyses. According to that report, the result of systematic retrospective review of regulations:

> should be a greatly improved understanding of the accuracy of prospective analyses, as well as corrections to rules as a result of ex post evaluations. A large priority is the development of methods (perhaps including not merely before-and-after accounts but also randomized trials, to the extent feasible and consistent with law) to obtain a clear sense of the effects of rules. In addition, and importantly, *rules should be written and designed, in advance, so as to facilitate retrospective analysis of their effects.*

While these executive orders apply only to the executive branch, President Obama has made it clear that independent agencies should adhere to the same retrospective review principles as executive branch agencies. In his subsequent Executive Order 13579, President Obama recommended that independent regulatory agencies, no less than the executive branch, should promote the goals of EO 13563:

To facilitate the periodic review of existing significant regulations, independent regulatory agencies should consider how best to promote retrospective analysis of rules that may be outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned.

In line with the requirements of EO 13579, OMB’s implementation memo, and OMB’s Draft 2013 Report to Congress, it is clear that both the executive and independent regulatory agencies issuing this rulemaking should incorporate specific plans for retrospective review and ex post evaluation into the text of its final rule.

**Retrospective Review Requirements**

To evaluate whether the Agencies’ proposal was “designed and written in ways that facilitate evaluation of [its] consequences,” we measure it against five criteria:

- Did the Agencies clearly identify the problem that their proposed rule is intended to solve?
- Did the Agencies provide clear, measurable metrics that reviewers can use to evaluate whether the regulation achieves its policy goals?
- Did the Agencies commit to collecting information to assess whether their measurable metrics are being reached?
- Did the Agencies provide a clear timeframe for the accomplishment of their stated metrics and the collection of information to support their findings?
- Did the Agencies write their proposal to allow measurement of both outputs and outcomes to enable review of whether the standards directly result in the outcomes that the Agencies intend?

**Identifying the Problem**

The first of the “Principles of Regulation” outlined by President Clinton in EO 12866 makes it clear that, as a first step, agencies must be able to identify the problem that justifies government action through regulation:
Each agency shall identify the problem that it intends to address (including, where applicable, the failures of private markets or public institutions that warrant new agency action) as well as assess the significance of that problem.

This step is crucial to the formulation of any policy. Without knowledge of the problem that the Agencies are trying to address, the public cannot assess whether a policy has had the intended effect, which is key in retrospectively evaluating regulation. In the text of the proposed rule, the Agencies fail to provide evidence of problems that require a regulatory solution or even specifically describe what problems they are attempting to address. Without outlining the purpose of the rule (or describing its potential cost and benefits) the Agencies simply refer to the statutory authority. In doing so, the rule does briefly explain the purpose of Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, the act which the Dodd-Frank Act amended in order to establish the Minimum Requirements to be applied by states; that purpose being, to provide

protection for federal financial and public policy interests in real estate related transactions by requiring real estate appraisals used in connection with federally related transactions to be performed in writing, in accordance with uniform standards, by appraisers whose competency has been demonstrated and whose professional conduct will be subject to effective supervision.\(^5\)

Also, according to section 1473 of the Dodd-Frank Act itself, the rationale for providing Minimum Requirements for AMCs is to establish a “consumer protection mandate” on the part of the ASC of the FFIEC.\(^6\)

Apart from this, there is no discussion of the problem that the rule is proposing to solve, such as whether the problem stems from “the failures of private markets or public institutions.” It is possible that the statute and regulations seek to address an asymmetry in the information available to consumers and those in the appraisal industry.\(^7\) However, without a clear

\(^5\) 79 FR 19537


\(^7\) OMB Circular A-4 identifies asymmetric information as a possible failure of private markets potentially warranting regulation, but it cautions agencies that “even though the market may supply less than the full amount of information, the amount it does supply may be reasonably adequate and therefore not require government regulation.” Relevant to this proposal, A-4 goes on to say, “when it is time-consuming or costly for consumers to evaluate complex information about products or services (e.g., medical therapies), they may expect government to ensure that minimum quality standards are met. However, the mere possibility of poor information processing is not enough to justify regulation. If you think there is a problem of information processing that needs to be addressed, it should be carefully documented.”

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identification of a problem, it will be difficult to measure how effective this rule is and to construct a successful plan for retrospective review.

Measurement Criteria

In order to measure the success of this rule following implementation, it is necessary for the Agencies to define what constitutes a “success.” As noted above, however, the Agencies have not identified the problems the rule would address, which hinders their ability to identify metrics of success. Of course, not all positive outcomes can be directly measured; however, many can be, and the proposed rule stage is the perfect time to introduce a plan to measure the rule’s effects to gauge its efficacy.

Before issuing a final rule, the Agencies should identify the outcomes they expect from it. Will the requirements in the rule lead to:

- More accurate appraisals?
- More timely appraisals?
- Lower cost appraisals?

They should also identify what metrics they could use to measure the extent these outcomes, or any others they identify, are achieved once the rule is in place.

Implementation of the rule may also have unintended consequences, which the Agencies should also consider in developing the proposal, and measure after the rule is issued. For example, the registration and licensing requirements may result in:

- A decreased supply of appraisal services, and a corresponding increase in consumer prices,\(^8\)
- Adverse effects on smaller appraisal firms, leading them to exit the market.

Information Collection

In order for retrospective review to be effective, the Agencies should identify how they will gather information to assess whether their stated metrics are being accomplished. Nowhere in this proposal do the Agencies describe how they might collect the relevant information to evaluate the rule after implementation. Consistent with the requirements of the Paperwork Reduction Act, the Agencies should commit to collecting the information needed to measure the rule’s success.

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8 Economic theory and evidence have shown that occupational licensing requirements restrict entry, thereby reducing competition and increasing prices. See, for example, S. David Young, *Occupational Licensing*, Lib. Of Econ. & Liberty, Jun. 5, 2014 http://www.econlib.org/library/Enc1/OccupationalLicensing.html

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**Timeframe**

The text of the proposed rule does not include a timeframe for retrospective review. In the final rule, the Agencies should identify a timeframe for review, indicating how soon after implementation they will begin to measure the progress of its stated metrics.

**Measure Linkages**

In the final rule, the Agencies should not only identify a set of metrics, but make clear how the measures they identify address the problems that the rule intends to solve.

As the Agencies commit to measuring the effects of this rule, they should also be aware of mediating factors that may have contributed to or undermined the stated metrics absent the rule. For example, a smaller supply of appraisers resulting from the licensing requirements could undermine the objective of reducing average processing time for home sales. Determining linkages between the Agencies’ rule and the measured outcomes is necessary to ensure that the policy itself resulted in the desired outcomes, rather than other factors beyond the Agencies’ control.

**Recommendations**

Before issuing a final rule, the Agencies should first clearly identify the problems the rule is designed to address. They should then identify what metrics could be used to evaluate the extent to which the rule achieves those intended outcomes. These outcomes might be improvements in the quality, timeliness, or costs of federally related transactions. The Agencies should also consider, and identify tools to measure possible unintended outcomes of the rule’s requirements, including less competition, higher prices, and adverse effects on small entities.

As drafted, the proposal does not comply with the requirements of Executive Orders 12866, 13563, and 13579 that agencies 1) “identify the problem that [they] intend to address (including, where applicable, the failures of private markets or public institutions that warrant new agency action) as well as assess the significance of that problem,”9 2) “assess all costs and benefits of available regulatory alternatives, including the alternative of not regulating,”10 and 3) “facilitate periodic review of existing regulations.”11

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9 E.O. 12866 Section 1(b)(1)
10 E.O. 12866 Section 1(a)
11 E.O. 13563 Section 6 and E.O. 13579 Section 2.