

# Ethics in the Appraisal Profession

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**W**hile most real estate appraisal work is accomplished by appraisers in an objective, unbiased, and ethical manner, self interest and selfish business choices will always be with us. Thus, appraisers must constantly identify ethical issues and refine ethical principles in the profession. Regardless of their upbringing or propensity to high professional standards, some appraisers still produce dishonest reports to satisfy their own or their client's interest or produce faulty reports as a result of ignorance, error or lack of effort. This was so 40 or 50 years ago and it remains so today.

There can be no professional justification for any appraiser—motivated by the desire to advocate for his client for monetary reasons or for other reasons of personal gain—to willfully and knowledgeably produce a dishonest appraisal.

For an appraiser to produce a faulty appraisal through ignorance, error, or lack of effort is just as inexcusable.

Faulty appraisals diminish respect for the appraisal profession. People tend to believe that all faulty appraisals are intentionally drafted because the appraiser seeks the reward of a high appraisal fee. This is not so. Undoubtedly, more appraisals are faulty because of lack of knowledge, skill, or application. This article will discuss the changing role of ethics today, covering both dishonesty and professional deficiencies, in contrast with the past.

#### ETHICS DEFINED AND APPLIED TO APPRAISERS

In its simplest terms, a violation of appraisal ethics is an act which has the potential of causing "damage" to another. To be unethical, an act does not necessarily have to do harm; it merely has to have the *potential* of doing harm as a result of unprofessional conduct by the appraiser. Herein lies one of the great pitfalls of some appraisers' thinking; that is, that an appraiser endeavors to determine if the unethical conduct will do harm (rather than asking whether it has the potential of doing harm). Since the entire appraisal profession (and, for that matter, all of business) is so much more complex today, there is more need than ever to define and adhere to ethical behavior which is in tune with contemporary professional standards. Proper behavior does not have the "built-in" potential of doing harm to others because of an improper act of the appraiser.

Appraisers deal mostly with empirical evidence. Because of this, some appraisers, by misuse of market data, can expose their true character in the performance of their work. The greatest evidence today of the merits of obtaining and keeping integrity can be found in the reputation of appraisers in every large city in the United States and in many small cities. Usually, people lacking a reputation for integrity or who are less than fully honest are not very successful.

Appraisers today have a more difficult time defining their ethical orientation. They may have a more difficult time recognizing the long-term benefits of total objectivity. Yet, they must endeavor to develop an attitude of importance toward their role in the economic picture which

will protect them from the various temptations to be unethical.

#### THINKING THROUGH ETHICS

The traps of improper appraisal ethics can be demonstrated in an analysis of mortgage loan appraisals. We consider unethical behavior mainly from the standpoint of the borrower in mortgage loan situations because, unfortunately, these are the most frequent instances of favoritism; little thought is expended on the failure to adequately value properties and the economic waste and personal harm low appraisals cause.

The fundamental reason for the services of the real estate appraiser in the business of mortgage loans, imposes tremendous responsibility on the appraiser: Statutes and regulations of government dictate that financial institutions with fiduciary responsibility protect the shareholders by obtaining an objective appraisal. If the appraiser's intention is to render an estimate of value on as objective and impartial basis as possible, regardless of the parties involved, then the appraiser's responsibility should not be a burden.

On a practical basis, here are the "big picture" considerations of the mortgage loan appraiser in estimating the value of the property to be offered as security for the mortgage:

1. The borrower can benefit financially if the transaction is completed.
2. The bank will benefit if it is able to make the loan.
3. If this is a sale, the vendor will benefit.
4. The local economy will benefit from either the new project or the existing project.
5. All of the above considerations depend upon a "satisfactory" appraisal by the appraiser.

Obviously, the trap in the above thinking is the lack of consideration of the damage that can be caused if the appraisal is improper, either too high or too low. Ethical considerations of mortgage loan appraisals today mainly focus on too-liberal appraisals which can cause considerable loss to the lender. The recent losses of the savings and loan associations and banks have focused attention on too-high appraisals.

In addition to possibly causing a loss to the lender, ultra-liberal appraisals may result in an unneeded and eventually defunct project becoming a drag on the local economy. Furthermore, such appraisals can cause financial ruin to the borrower. Rather than

benefit the borrower, the appraisal facilitates his downfall. Therefore, particularly in light of recent history of financial institution failures, it is more important than ever not to overestimate the value of the collateral.

Conversely, there is a very significant aspect of ethics involved in underestimating collateral. If an appraiser kills the deal by being unreasonably conservative, he causes an economic loss by frustrating economic progress. When the Resolution Trust Corporation was disposing of properties at bargain-basement prices, this tended to depress markets and to convert appraisers into what I refer to as "submarine commanders," meaning they appraised all properties very low. Many were unable to ascend to more realistic values once the RTC influence was gone and the market returned to normal.

#### SOPHISTICATED UNETHICAL BEHAVIOR

Decades ago, a prominent appraiser in our area advocated a high unit price of say \$1,000 per acre for a rural sugar cane farm through which a pipeline was proposed. The total tract was over 1,000 acres. Value at the time likely approximated \$275 per acre. The matter was litigated and the appraiser's value opinion became public knowledge. Unfortunately, the owner died a few months later. The value of the land for estate tax purposes was placed at \$225 per acre by this same appraiser. The appraiser had great difficulty justifying his value of \$225 per acre to the IRS. Today, such behavior could lead to dire consequences.

Oversight mechanisms since that time make it considerably more difficult to make faulty appraisals, either too high or too low. State appraisal licensing and certification, with their respective Uniform Standards of Professional Practice<sup>1</sup>, contain the possibility of loss of the right to practice. Standards require that appraisal reports must be in writing or that the appraiser have support in the files. The appraisal report (or the files) must contain the data and logic upon which the value is estimated. Additionally, there are penalties in the Internal Revenue Code for some flagrant advocacy appraisals.<sup>2</sup>

#### ADVOCACY INSTEAD OF OBJECTIVITY

But, along with the above progress in regulating the profession and the more complex economic conditions today,