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AIREA Research Series

Impacts of Regulation On the Appraisal Industry

Research Report 2

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Part II -- REGULATORY INITIATIVES FOR INDUSTRY

Schultz: The next presenter is James A. Graaskamp speaking on "Can the Appraisal Industry Survive without Increased Regulation?"

Graaskamp: The question is, I think, a little ephemeral. I think most industries have found that once they get over the shock of what they perceive as government interference with their industry, government regulations adroitly exploited have been a great advantage to the industry. Either they establish a monopoly for them or they shield them from the consumer, or at least greatly narrow the parameters of the unknown as to where their responsibility in their process lies. So I think initially one does not have to regard regulation as a singularly negative concept.

Now I would like to divide the question of whether the appraisal industry can survive without it into essentially three areas, looking at regulation as protective rather than as pejorative. The first major factor that accounts for the appraisal profession being uncomfortably ill is its customer base. Historically, the appraisal industry has been unable to protect itself from its own customers. If R-41c has anything to say for itself, it is the fact that it makes the customer, as the fiduciary hiring the appraiser and applying the appraisal in his or her lending and realty process, equally culpable for an inappropriate or incomplete piece of work. It is now in his or her vested interest that you should be allowed to operate as a professional.

That type of regulation is a very positive element, and to define it as part of the regulatory environment of appraisals certainly is to be encouraged. How do we protect ourselves from our best friends, namely, our customers, who have gone a long way toward destroying the credibility of the appraisal process? The American tradition of reciprocity, of advocacy and the team approach, is very hard to overcome whether you are in a law case or a loan case. The measure of success is, Did we get the loan? The fee system has traditionally enhanced it; more frequently one is hired by the applicant for the loan than by the lender, and then there is the matter of all parties working for community development. This very parochial type of relationship in many cases is virtually an implied conspiracy between the lender who wants to make a loan under any circumstances, and the developer who needs the loan under any circumstances, and the appraiser who wants to be part of the "good ole boy" network that carries this off.

So regulation protects us from our best friends, but I don't think we can survive without it. I think making the customer equally culpable with the appraiser for a poor piece of work, as evident in R-41c, is a very positive regulatory step.

The second area of increased regulation concerns what Mr. Harrington was talking about today. I think the appraisal is a critical social function for equity in our society. Whether we're talking about the protection of our financial institutions, about the relationships between two parties attempting to achieve a fair contract, or about eminent domain and public compensation, the appraisal product should be the pivotal issue rather than the appraisal process. The appraisal process too often is manipulated today against the advocacy positions of the usual vested interests. To the degree that increased regulation could better control the appraisal product so that it performed its critical function of social equity, then regulation advances the interest of professionalism in the appraisal process.

The third and perhaps most significant area in which regulation is a positive factor to the survival of the appraisal industry lies in the historical success of the appraisal process. There is a tremendous financial vested interest in the status quo, which is unfortunate in a society moving as quickly as Mr. Harrington has suggested this morning. We're moving toward a much higher level of social responsibility on the part of enterprise to society and to individual property owners. The social transaction is beginning to take precedence over the business transaction. The appraisal process has not kept up with that, and there are vested interests that do not wish to keep up with that. This renders the education of all of us in this room, let alone the entire professional cadre of appraisers, obsolete.

It obliterates a very significant investment of personal entities and money and time. Obviously, some would much prefer the status quo and a broader array of exemptions, disclaimers, shifts of liability to other professions, and so forth. The threat of new legislation and the related spin-offs of Congressional investigation of the collapse of the Sunrise Savings and Loan Association of Florida show the rate at which we've accelerated consideration of these issues.[23] Without that spur of regulation, there would not be a creative response to bridge the gap between social and business responsibilities.

Regulation is the only way in which we can break the inertia of the financial success of the appraisal process and force the responsible appraiser to come to grips with change in the business environment in which he or she works.

So for all these reasons, the appraisal industry not only cannot survive without regulation, but regulation provides the most accelerated means to move the industry into what essentially is the twenty-first century of professional response. Since we are a pivotal factor in a legitimate transaction and ours is a society in which the social transaction is now bearing equal weight with the business transaction, I don't see any way in

[23]For additional information see "Impact of Appraisal Problems on Real Estate Lending, Mortgage Insurance, and Investment in the Secondary Market," House Committee on Government Operations, 99th Cong., 2nd sess., H. Report 99-891, 1986, pp. 16-23.

which the appraisal industry can adapt without regulatory protection.

The final element is simply the cost of regulation itself. I think the appraisal industry has found it has not been able to afford self-regulation. It cannot afford it for several reasons. One obvious reason is the legal cost of due process associated with removing designations from those who have failed their responsibilities. Another is an internal cost in energy to the organization that has to spend so much of its resources disciplining its own members. This becomes very divisive and makes it difficult to go forward with the more positive aspects of this profession.

The punitive aspects of regulation within the profession should be divorced from its fraternal and educational functions so that the great majority can work together. Other industries have managed to insulate themselves from certain disagreeable functions, from inertia, and from their customers who otherwise would kill them with love and fees.

~~<u>Schultz</u>: Thank you, Dr. Graaskamp. Our next presenter this morning is William Pittenger of the Federal Home Loan Bank of Atlanta, speaking on "FHLBB Initiatives Affecting Appraisal."~~

~~<u>Pittenger</u>: Thank you, Carl. I've been asked to talk about the Board's perspective of regulation, including the history of~~