



Testimony of J. Scott Robinson, MAI, SRA, AI-GRS
Proposed Conflict of Interest Rule, Proposed Exemptions and
Regulatory Impact Analysis
August 13, 2015

Thank you for the opportunity to testify on behalf of the Appraisal Institute, the world's largest association of real estate appraisers¹. My name is Scott Robinson. I am the 2015 President-Elect of The Appraisal Institute.

Real estate appraisals play an important role in protecting pension plans that invest in real estate. Appraisals prepared by designated members of the Appraisal Institute and other valuation professionals are frequently used for financial reporting purposes. Such appraisals are prepared on a quarterly or annual basis, with such information frequently included in financial disclosures. We appreciate the consideration that has been given to our input on this type of appraisal service.

Another way that pension plans may use appraisals is when deciding whether to purchase or sell assets or when investments are moved in and out of plans. While we agree with the general intent of the proposed rule, we remain deeply concerned that the proposal will unnecessarily increase costs on consumers and users of appraisal services in important buy and sell decisions relative to plan investments.

¹ The Appraisal Institute is a global professional association of real estate appraisers, with nearly 21,000 professionals in almost 60 countries throughout the world. Its mission is to advance professionalism and ethics, global standards, methodologies, and practices through the professional development of property economics worldwide.
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Specifically, in its proposed rule, the Department has exempted the former from the proposed Fiduciary standard, but retains the inclusion of the latter, meaning, an appraisal firm who does financial reporting appraisals for a pension plan would not carry a fiduciary responsibility, but one doing appraisals for buy/sell decisions would be considered as a Fiduciary. Under the proposed rule, we could also see investors claiming an appraisal for loan (say to an LLC that served as the investment vehicle for 401k or IRA investments) was "in connection" with the transaction. The proposed rule, as is, clearly increases liabilities on real estate appraisers, and at the worst time – when the profession already faces challenges in attracting the next generation of valuation professionals.

Our concerns stem primarily from the lack of distinction between “appraisals” prepared for investment managers and “fairness opinions.” These are two completely different services, with their differences being central to questions about responsibilities to plan investors. Specifically, the proposed rule confuses the role of appraisals in buy and selling decisions; as the role of fiduciary is maintained by the investment manager, not the appraiser. The investment manager considers the appraisal, and compares that with other information (such as offers made on property), to make determinations in the best interest of the fund. The appraiser does not carry that responsibility or decision making authority, and contrary to the proposed rule, performs such work in accordance with generally accepted appraisal standards without advocacy to the client, or conflict of interest. This mandate is specifically addressed in both the USPAP Ethics Rule and the Appraisal Institute’s Code of Professional Ethics². Once the appraiser has completed the valuation assignment, fairness opinions may be developed by the investment manager or third party, who holds the fiduciary decision responsibilities regarding the transaction. The current version of the proposed rule mentions “appraisals” and “advice” in the same sentence. It is not the role of the appraiser

² Available at http://www.appraisalinstitute.org/assets/1/29/CPE_w_explanatory_comments_effect_01-01-15.pdf

to advise a client. The role of the appraiser is to provide their client with information that can be analyzed for the purposes of use of that asset within the plan.

An example of an unintended consequence of this proposal is found within the fact that a key part of an appraisal is identifying the intended use and intended users of the appraisal. The intended use and intended users gives the appraiser the ability to develop a scope of work appropriate for both. This proposal would create a potential unlimited number of intended users of the appraisal. This casts a wide net of liability onto the appraiser.

In contrast, fairness opinions differ vastly from appraisals, as they essentially represent the work an investment manager might perform as a third party. Fairness opinions answer a different question than appraisals. While appraisals may provide information to an investment manager or answer whether the value of the property is within a stipulated range of a price, it does not answer the question as to whether the price or the terms are “fair.” Such opinions *can* be offered by appraisal professionals, but such a service would not be considered an “appraisal.” This is an important distinction that is currently not found in the proposed rule, but is essential for any final rule.

We have consulted with professional liability insurance providers to the appraisal profession, and such a change will likely compound the difficulty in finding coverage for this type of service, or result in an increase in costs for valuation firms providing services. Most insurance policies to appraisers exclude ERISA-related claims, so coverage is difficult to obtain already. While plans such as those endorsed by the Appraisal Institute provide this coverage, we expect that the increased liability created by the proposal would have a corresponding effect on insurance costs.

Unfortunately, this will likely cause some to reconsider providing such important services, altogether. This is needless and unnecessary, as the DOL still has not provided clear evidence for why appraisers should be covered under the fiduciary definition. To our knowledge, the DOL has not attempted bringing enforcement actions against real estate appraisers, and has not explained how the process is weakened by the lack of fiduciary coverage. Further, the real estate appraisal profession has an ever-present regulatory structure, where public interests are actively protected. In fact, real estate appraisal is one of the most highly regulated professions in financial services, through state licensing and certification and federal oversight. Valuation professional organizations such as the Appraisal Institute maintain active ethics and standards enforcement. In contrast, the realm of fairness opinions is less defined and not subject to regulation similar to that seen in real estate appraisal.

We urge the DOL to resolve these concerns by undertaking two specific actions in any final rulemaking: 1) provide clear definitions for *appraisals* and *fairness opinions*, and 2) provide an exemption for appraisals prepared for specific transactions involving the acquisition, disposition or exchange of real estate. Doing these would distinguish fairness opinions, whether provided by appraisers or others, as carrying a fiduciary responsibility – a position that is reasonable given the purpose of the fairness opinion.

Thank you again for the opportunity to testify. I would be happy to answer any questions that you may have and offer to provide additional assistance the Department works toward the intent of the proposal, which is to ensure high quality real estate appraisals.