Surviving the Appraiser Shortage

Attorneys who need to meet minimum appraisal and appraiser requirements in their practices have various options

MANY individuals, businesses, and lawyers in California require real property appraisals for matters such as refinancing, real estate transactions, divorce, estate tax, and eminent domain actions. However, there is a shortage of real estate appraisers in California and throughout the United States. California’s Bureau of Real Estate Appraisers (BREA) has noted a 50-percent decline in the number of licensed appraisers in California over the past seven years. At present, there are 3,300 commercially licensed real estate appraisers in California. The state currently is issuing approximately 360 new licenses annually in California. Almost two-thirds of the appraisers in California are over age 50 and many are contemplating retirement. At the same time, the number of owner households is expected to increase by 1.3 million per year.

Industry experts identify several reasons for the decline in the number of appraisers. Stringent new education requirements that went into effect in 2015, a large increase in the required number of closely monitored experience hours, and lower fees have made real property appraising a less attractive profession. In addition, while the number of appraisers is declining, the number of complaints filed against appraisers by the general public is increasing exponentially.

Legally, what is an appraisal? Who is an appraiser? When is an appraisal required? The answers depend on the situation and type of assignment for which the appraisal is being used. Attorneys should be aware of who can perform appraisals, who can testify as to value, and what an appraisal must contain. Attorneys also should be aware of the various alternatives to formal appraisals.

Recently, it has been codified that certain transactions involving real property may proceed without obtaining a formal appraisal. This position is in direct contrast to that made by governmental agencies a few years ago when the issue focused on greater standards and more thorough accountability.

While appraisal standards are not new, they came to the forefront as a result of the savings and loan crisis of the 1980s. Appraisers were said to be part of that scandal since many appraisals were found to be inad-
equally or unfairly biased. In April 1989, as a result of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA), uniform standards for appraisers were formalized. These standards were to be enforced by each state’s real estate appraiser regulatory agency.

As a direct result of FIRREA, government and nongovernment agencies attempted to determine what these standards were and to define the terms “appraisal” and “appraiser.” However, despite numerous attempts the answer is still not clear. Further, there is much inconsistency in application. (See chart.)

The initial goal was to make appraisals “independent, consistent and objective.” The implementation of new standards and licensing requirements, however, had the indirect effect of reducing the number of appraisers. As a result of large barriers to entry, competition from nonappraiser alternatives, low fees, and other factors, the number of appraisers has steadily decreased. In 2015, for example, only 55 new trainee appraisal applications were filed for the entire state of Illinois. As a result of these new standards, which all states have adopted, the number of appraisers nationwide has declined substantially and will continue to decline.

Options for Attorneys

Attorneys who need to meet minimum appraisal and appraiser requirements for their legal work have several options. Real estate brokers, for example, frequently give broker opinions in estate planning matters. Accountants typically provide valuations and testimony in family law matters. Sometimes property owners will arrive at their own values. In addition, the word “valuation” (which is different from an appraisal) has come into play. An evaluation is not required to comply with the qualifications and reporting standards of appraisals under certain circumstances. (See chart.) These informal methods of appraisal may or may not be acceptable.

California is not a mandatory license state, which means certain types of valuations can be performed by nonlicensed individuals. Other times, performing an appraisal without a state license can lead to a fine and imprisonment. The line can be blurred at times. In California, a licensed appraiser is required in any transaction in which a federal financial institution’s regulatory agency engages, contracts, or regulates, and which requires the services of a state-licensed real estate appraiser.

What about the other reasons for an appraisal? The courts in California and the federal government have been forced to decide the question of who is qualified to evaluate real property and when an appraisal is required. One specific exception to appraisals is for broker opinions in which a person licensed to sell real property under the California Department of Real Estate provides an estimate of value.

Appraisal Licensing Requirements

<table>
<thead>
<tr>
<th>PURPOSE</th>
<th>LEGAL REQUIREMENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lending (under $250,000)</td>
<td>No appraisal required†</td>
</tr>
<tr>
<td>Federal Bank</td>
<td>License probably required²</td>
</tr>
<tr>
<td>Family Law</td>
<td>Anyone, including spouses³</td>
</tr>
<tr>
<td>Eminent Domain</td>
<td>Property owners and qualified experts⁴</td>
</tr>
<tr>
<td>Charitable Gifting–noncash over $5,000</td>
<td>Licensed appraiser required⁶</td>
</tr>
<tr>
<td>Probate</td>
<td>No license required, probate referee or conservator⁶</td>
</tr>
<tr>
<td>Property Tax</td>
<td>Licensed or certified appraiser⁷</td>
</tr>
<tr>
<td>Estate and Gift</td>
<td>No license required, minimum standards⁸</td>
</tr>
<tr>
<td>Litigation Evidence</td>
<td>No license required, goes to weight⁹</td>
</tr>
</tbody>
</table>

**INSTRUCTIONS FOR OBTAINING MCLE CREDITS**

1. Study the MCLE article in this issue.
2. Answer the test questions opposite by marking the appropriate boxes below. Each question has only one answer. Photocopies of this answer sheet may be submitted; however, this form should not be enlarged or reduced.
3. Mail the answer sheet and the $20 testing fee ($25 for non-LACBA members) to:
   Los Angeles Lawyer
   MCLE Test
   P.O. Box 55020
   Los Angeles, CA 90055

Make checks payable to Los Angeles Lawyer.

4. Within six weeks, Los Angeles Lawyer will return your test with the correct answers, a rationale for the correct answers, and a certificate verifying the MCLE credit you earned through this self-assessment activity.

5. For future reference, please retain the MCLE test materials returned to you.

**ANSWERS**

Mark your answers to the test by checking the appropriate boxes below. Each question has only one answer.

<table>
<thead>
<tr>
<th>Question</th>
<th>True</th>
<th>False</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>11.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>12.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>13.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>14.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>15.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>16.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>17.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>19.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>20.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Specifically, the law states that the term “appraisal” does not “include an opinion given by a real estate sales licensee or engineer or land surveyor in the ordinary course of his or her business in connection with a function for which a license is required.” Thus, an exception to the Business and Professions Code requiring appraisers to be licensed has been carved out in certain circumstances.

The California Evidence Code generically discusses the issue of expert opinions. It states:

If a witness is testifying as an expert, his testimony in the form of an opinion is limited to such an opinion as is: (a) Related to a subject that is sufficiently beyond common experience that the opinion of an expert would assist the trier of fact; and (b) Based on matter (including his special knowledge, skill, experience, training, and education) perceived by or personally known to the witness or made known to him at or before the hearing. …

The issue of whether or not a valuation opinion is admissible is of a type that reasonably may be relied upon by an expert in forming an opinion upon the subject to which his testimony relates, unless an expert is precluded by law from using such matter as a basis for his opinion. DuPont v. Merrell Dow Pharmaceuticals clarified Federal Rules of Evidence Section 720 and stated that the judge is the gatekeeper as to expert witness testimony. In an unpublished case, Johnson v. Dawkins, the court stated that the absence of a real estate license goes to the weight of testimony, not to whether the testimony can be admitted: “The absence of a license at best went to the weight of his testimony, there is no requirement that one be licensed in California to give expert testimony as an appraiser.”

The courts have dealt with the issue of what constitutes an appraisal and an appraiser in several situations, including tax matters, probate, gifts, and various aspects of family law. With respect to tax matters, the federal government provides guidance in Section 2 of Internal Revenue Bulletin 2006-46, which relates to the appraisal requirements for types of noncash charitable contributions. The document states that for an appraiser to be qualified to value noncash charitable contributions over $5,000, he or she must be “an individual who (1) has earned an appraisal designation from a recognized professional appraisal organization or has otherwise met minimum education and experience requirements set forth in regulations prescribed by the Secretary, (2) regularly performs appraisals for which the individual receives compensation, and (3) meets such other requirements as may be prescribed by the Secretary in regulations or other guidance.”

The bulletin further provides that “an individual will not be treated as a qualified appraiser unless that individual (1) demonstrates verifiable education and experience in valuing the type of property subject to the appraisal, and (2) has not been prohibited from practicing before the Internal Revenue Service.”

A seminal case of a tax nature involves the question of who is a qualified appraiser. In Estate of Richmond, the executors of an estate hired the taxpayer’s certified public accountant to perform entity appraisals for submission on an estate tax return. The IRS complained that the taxpayer’s appraiser was not qualified. The Tax Court agreed and imposed not only the taxes, penalties and interest but also a 20 percent “accuracy-related penalty” for a “substantial estate tax valuation understatement.” The court ruled that despite being a CPA with a master’s degree in taxation, and having written 10 to 20 valuation reports, some of which he testified to in court, he was not qualified as an expert. As a disclaimer, the accountant was providing an opinion as to the value of a business and not real property.

California requires assets subject to probate to be valued by a probate referee (formerly, an inheritance tax appraiser). Probate referees are allowed under the California Probate Code. They are required to be either appraisers, accountants or attorneys. This differs from Estate of Richmond in which the court stated that an accountant was not a qualified appraiser to value business interests in an estate tax setting. However, there is a question as to whether a probate referee can provide a qualified appraisal for tax purposes under Internal Revenue Bulletin 2006-46 since a qualified appraiser under the Code of Federal Regulations is defined as an individual who has earned an appraisal designation from a recognized professional appraiser organization and regularly performs appraisals. The California Probate Code allows another exception to Business and Professions Code Section 11302 (b) to allow probate referees to provide appraisals in probate matters. On the other hand, there is no clear guidance as to whether probate referees can provide valuations on nonprobate matters such as estate taxes or eminent domain cases.

Regarding gifts, the Department of Treasury issued Publication 561 in 2007, which states that any noncash donation to a qualified charity over $5,000 requires a qualified appraisal by a qualified appraiser. The definition of qualified appraiser includes one who is licensed to value property in his or her state. Hence, for the valuation of a noncash real estate gift to a qualified organization, it appears that only licensed real property appraisers can value the asset.

In family law, each spouse has an interspousal duty to accurately value assets. The courts call for the fair and equitable disposition of assets. The court in one case said nonbinding arbitration between the two spouses could not be used to determine value. For community property assets:

In family law proceedings, the value of real property may be established by evidence other than expert appraisal. The court in In re Marriage of Folb discussed using lending appraisals as well as recent sales of the property as evidence of value. Essentially this is left up to the trier of fact.

Can a spouse prepare an appraisal on his or her property? “The property owner or owner’s spouse is competent to testify as to the value of his or her own property even though not qualified to testify as an expert.”

Opinion of Value Evidence

The issue of who may provide evidence of value has been dealt with numerous times, most notably in the U.S. Supreme Court case of Daubert v. Merrell Dow Pharmaceuticals. The Daubert case is found to apply to California cases via Sargon Enterprises, Inc. v. USC. Moreover, valuation evidence also has been addressed in California Evidence Code Sections 810 to 824.

California Civil Jury Instructions Section 3501 discusses what an appraisal is and how a jury should weigh the issue of value. Further, the court in Alles v. Hill determined the property owner was also a real estate broker and the issue of competence was a matter of fact. Further, the trier of fact should determine whether the expert met the qualifications of Evidence Code Section 813. Finally, in Daubert, the court becomes the “gatekeeper” to ensure that the scientific methodology upon which the expert opinion is founded is reliable.

In eminent domain cases, the only type of evidence that can be used to establish value is the opinion of qualified experts and property owners. Evidence Code Sections 810 to 813 are said to apply specifically to eminent domain cases.

Evidence Code Section 813 provides that the value of property may be shown only by
You Are Invited

34TH ANNUAL RED MASS
An Ecumenical Event for the Legal Community of All Faiths and Traditions

Wednesday, November 9th, 2016 at 5:30 PM
Cathedral of Our Lady of the Angels • 555 West Temple Street, Los Angeles

Celebrant: Archbishop José H. Gomez • Homilist: Reverend James L. Heft, S.M.

Hosted Reception to Follow
DISTINGUISHED SPONSORS

Lewis Roca
Rothgerber Christie

Morgan Lewis

MCKOOL SMITH
HENNIGAN

POLSINELLI

BENEFACTORS
Andrade Gonzalez, LLP • Carlsmith Ball LLP • DTI • Michael Scott Feeley, Esq.
George Ignatius Foundation • Lawrence P. Grassini, Esq. • Greenberg Traurig LLP
Hueston Hennigan LLP • Gustavo Lamanna, Esq. • Morrison & Foerster LLP
Panish Shea & Boyle LLP • Matthew Mark Pope, Esq. • Sedgwick, LLP
Seyfarth Shaw LLP • Peter Sullivan, Esq. • Michael Zea - Ringler O.C.

PATRONS
Oscar A. Acosta, Esq. • Martin R. Boles, Esq. • Hon. Lawrence Crispo • ForensisGroup
Margaret Graf, Esq. • Hidalgo, A Law Corporation • Nancy L. Iredale, Esq.
Hratch Karakachian, Esq. • Kneafsey & Friend LLP • Mancini & Associates • Phillip R. Marrone Esq.
Steven A. Mindel, Esq. • Paul Tosetti, Esq. • William W. Wardlaw, Esq.

SPONSORS
Mark Anchor Albert, Esq. • Margaret Ambrose, Esq. • Suzanne L. Austin, Esq. • Joseph M. Barrett, Esq.
Carmela Bombay, Esq. • Kevin Boyle, Esq. • Kevin Brogan, Esq. • Hon. Richard Byrne (ret) • Patrick Cain, Esq.
Stuart Chapman, Esq. • George Crook, Esq. • Lawrence W. Dailey, Jr., Esq. • Sylvan P. Daroca, III, Esq.
Robert Ebner, Esq. • William Emanuel, Esq. • Vince Farhat, Esq. • Allan Graf, Esq. • George Hawley, Esq.
John Hilson, Esq. • Italian American Lawyers Association • Robert Keane, Esq. • Michael Kelley, Esq.
Philip F. Lanzafame, Esq. • Marina Macchiagodena, Esq. • Michael M. Maddigan, Esq. • Michael Maloney, Esq.
Patrick McLaughlin, Esq. • Robert Miller, Jr. Esq. • Nicolas Nassif, Esq. • Michael Norris, Esq.
Michael O’Connor, Esq. • Brian Panish, Esq. • David Plumley, Esq. • William Pao, Esq.
Gina Pech, Esq. • Alma Puente, Esq. • Richard Reyes, Esq. • Gregory Salvato, Esq. • Rickard Santwier, Esq.
Prof. Daniel P. Selmi, Esq. • Adam Shea, Esq. • Paul Smith, Esq. • Margaret Stevens, Esq.
Carole Viola • Molly M. White, Esq. • Prof. Scott Wood, Esq.

Donor list is current as of publication. For a complete list of donors, please visit our website at laredmass.org

The Red Mass is a centuries-old tradition recognizing the legal and judiciary communities

Sponsored by the St. Thomas More Society of Los Angeles
the opinions of witnesses qualified to express such opinions and of the owner of the property being valued. Evidence Code Section 813 applies only to eminent domain and inverse condemnation proceedings by virtue of Evidence Code Section 810.55

Options to a Formal Appraisal

Most real property appraisers say that the future of the industry lies in appraisal management companies (AMCs).58 Most appraisers are unhappy with AMCs because they have had the effect of reducing appraisal fees and increasing deadlines.59

An AMC is essentially an administrative entity that procures appraisals by licensed appraisers. It is not in and of itself a licensed appraiser. The BREA issues approximately 125 new AMC licenses per year.60

Business and Professions Code Section 11302 (d) (1) defines an AMC as “an “appraisal management company,” which means any person or entity that satisfies all of the following conditions:

(A) Maintains an approved list or lists, containing 11 or more independent contractor appraisers licensed or certified pursuant to this part, or employs 11 or more appraisers licensed or certified pursuant to this part. (B) Receives requests for appraisals from one or more clients. (C) For a fee paid by one or more of its clients, delegates appraisal assignments for completion by its independent contractor or employee appraisers.

Appraisers do not like AMCs because they search for appraisers who can produce the valuation at the lowest cost and quickest turnaround. Lenders like AMCs for the same reasons. Appraisers say they feel as if they are being asked to perform appraisals in a less than fully competent manner and for a reduced price. On the other hand, this is another reason that fewer appraisers are entering the market.61

Another alternative to formal appraisals is automated valuation models (AVMs). These are computer-generated appraisals provided on online real estate data bases, for example Zillow, Trulia, and RealQuest. When a user inputs a home address on Zillow, a value is generated using computer models that require no human input. Some companies now are writing software to perform advanced commercial real property appraisals.

An evaluation is a transaction that does not require the services of a state-certified or licensed appraiser.62 The Federal Register states that “while licensed or certified appraisers may be qualified to perform evaluations, the agencies do not believe these appraisers are the only persons that can render a competent estimate of the value of real estate for exempt transactions.”63

This is another area in which consumers are opting for low-priced appraisals. Some valuation firms are turning to hiring personnel in India, China, and other countries in which labor costs are low. There may or may not be an actual property inspection, but a real person addresses valuation issues and writes reports. A licensed appraiser may or may not sign off on reports, but the reports give the appearance that a real person addressed the valuation.

In 2012, as a result of the shortage of appraisers and the backlog of valuations preventing loans from closing on time, federal financial regulators came up with the term “de minimis valuation thresholds.”64 This is a $250,000 threshold below which an appraisal is not required for a federally related transaction.

Last year, the Federal Financial Institutions Examination Council, FDIC, and the American Bankers Association considered increasing the amount of a de minimis valuation threshold to $500,000. However, various appraisal associations opposed this action, saying it would have a negative impact on real estate lending practices. In fact, some appraisal organizations have proposed lowering the threshold to $25,000.65 In many states (other than California), homes can cost significantly less than $250,000. Therefore, the need for appraisers in those states has declined.

The appraisal industry has come full circle.
What was intended as a way to make appraisers more competent and objective has turned into the use of automated valuation models, appraisal management companies, and de minimis valuation requirements. The direction appears to be away from mom-and-pop appraisers toward administrative entities and computer-generated valuation models as consumers of appraisals look to innovative ways to get their properties appraised.

1 Unless mentioned otherwise, all references to appraisers shall refer to licensed real property appraisers.
2 Background Paper, Joint Oversight Hearing, Bureau of Real Estate Appraisers, No. 6, 13 (March 9, 2016) [hereinafter Background Paper].
3 The Appraiser Shortage, What Can Be Done?, APPRAISAL BUZZ (March 8, 2016).
5 The number of real estate appraisers is falling. Here’s why you should care, MARKET WATCH (Nov. 18, 2015).
6 The Real Property Appraiser Qualification Criteria (Jan. 1, 2015).
7 Background Paper, supra note 2, at 10.
8 See 12 C.F.R. §34.43.
9 12 C.F.R. §§34.43-.44.
11 Id.
12 See, e.g., THE APPRAISAL FDN., 2016-2017 UNIFORM STDS. OF PROF’L APPRAISAL PRAC., 6, 151 [hereinafter USPAP].
13 Id.
14 Isaac Peck, The Disappearing Appraiser, WORKING RE, (Spring 2016) [hereinafter Peck].
15 PENAL CODE §1170.
16 BUS. & PROF. CODE §11302 (j).
17 USPAP, supra note 11.
18 USPAP, supra note 11, at 1.
19 Id.
20 BUS. & PROF. CODE §11319.
21 USPAP, supra note 11, at 1, 105, 141.
22 BUS. & PROF. CODE §11302.
23 Id.
24 BUS. & PROF. CODE §11319.
25 Id.
26 USPAP, supra note 11, at 1, 105, 141.
27 BUS. & PROF. CODE §11302 (b).
28 Id.
29 EVID. CODE §801.
31 Id.
33 See also I.R.C. §170(f)(11)(E)(ii).
35 Id. at 46.
36 Id. at 13. As a disclaimer, this case applied to specific facts. The reader is encouraged to read the particulars of this case.
37 PROB. CODE §§8900-8909.
38 Id.
40 BUS. & PROF. CODE §11302(b); see also PROB. CODE §§400-08.
41 See Code Civ. Proc. §873.010
46 EVID. CODE §§813(a)(2), (c); 814.
48 Sargent Enters., Inc. v. Univ. of S. Cal., 55 Cal. 4th 747 (2012).
49 EVID. CODE §813(a)(1)(2)(3).
51 Daubert, 509 U.S. 579.
53 Folb, 53 Cal. App. 3d at 870.
55 Evaluations are defined in the document Interagency Appraisal and Evaluation Guidelines, revised June 7, 1994.
56 12 C.F.R §34.43.
57 Banking in the Ninth, supra note 54.
58 Peck, supra note 14.
59 Id.
60 Background Paper, supra note 2, at 10.
61 Peck, supra note 14.
62 Id. at 7.
63 12 C.F.R §34.43 (b).
64 See, e.g., 12 C.F.R. §34.43; Fed. Reserve Sys. §225.63(b); Office of Thrift Supervision §564.3(b) [Office of the Comptroller, Fed. Res. Sys].