

# THE OPINION OF THE COLLEGE ON

## Appraisal Practice: Contractual and Fiduciary Relationships; Lawsuit; Mediation

Initiation, Chair Responsibility,  
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In July 1990, the American Society of Appraisers amended Section 3.6 of its Code of Ethics. The section follows (emendation in italics).

### 3.6 Appraiser's Fiduciary Relationship to Third Parties

It frequently happens that an appraisal report is given by the client to third parties for their use. These third parties may or may not be known to the appraiser but, regardless of this fact, they have as much right to rely on the validity and objectivity of the appraiser's findings as does the client *for the specific stated purpose of the intended use for which the appraisal was originally made*. Members of the Society recognize their fiduciary responsibility to those parties, other than the client, who made use of their reports.

There are few examples that better illustrate contractual and fiduciary relationships to third-party factors than the unique San Diego, Calif., lawsuit of *Gay v. Broder*, 109 Cal. App. 3d 66; 167 Cal. Rptr. 123; Civ. No. 22162, Fourth Dist., Div. One, Aug. 11, 1980. The issues involved are considered to be of first instance in California. The case "summary" is instructive. It is quoted not only to establish the legal environment of the lawsuit but to introduce a concern that the College feels to be of first importance to practicing appraisers: What measures, in addition to maintaining high educational, experience, and ethical criteria, may be undertaken by appraisers to best safeguard contractual and fiduciary relationships? What additional safeguards may an appraisal society advise its members to consider in order to achieve and sustain a worthy public perception of the integrity of the practitioner and the appraisal process? The summary:

A veteran whose application for a Veterans Administration guaranteed home loan to finance his purchase of a home was denied brought an action against the appraiser who had inaccurately appraised the home at less than its reasonable value and who had allegedly thereby caused a denial of the veter-

an's application for the guaranteed loan. The veteran's complaint alleged the appraiser was liable to the veteran for the monetary damages he sustained as the result of the denial of his application for the loan on the basis of contractual liability and on the basis of the appraiser's negligence in submitting an inaccurate appraisal. The action was dismissed after the court sustained a demurrer to the complaint by the appraiser. (Superior Court of San Diego County, No. 418305, Edward T. Butler, Judge.)

The Court of Appeal affirmed. The Court held that the statute regulating the Veterans Administration home loan guarantees [38 USC Sec. 1810 (b) (5)] was for the protection of the Veterans Administration rather than for that of a veteran seeking a Veterans Administration guaranteed home loan, that judicial notice of the statute controverted the allegation in the veteran's complaint that the appraiser's agreement with the Veterans Administration to appraise the home that was the subject of the veteran's application for a guaranteed loan was made for the benefit of the veteran, and that there was no showing of any privity of contract to support any contractual liability on the part of the appraiser to the veteran for the appraiser's inaccurate appraisal. The appraiser was therefore not liable for any monetary damage sustained by the veteran as the result of his negligence in submitting an inaccurate appraisal. (Opinion by Lord, J., with Cologne, Acting P.J., and Staniforth, J., concurring).

The Opinion contains a review of three causes of action. The first cause of action is particularly helpful in describing the factual conditions:

In March 1978, Gay, a veteran, applied for a home loan on property on Devon Square in San Diego. The application was made to Home Federal Savings and Loan Association and the loan was to be guaranteed by the Veterans Administration, an agency of the United States. Upon such application the Veterans Administration has a statutory duty to make an appraisal of the property and may appoint a designated fee appraiser to do so. Michael A. Broder, a designated fee appraiser, entered into an agreement with the Veterans Administration to make the appraisal to determine the amount of the loan to be guaranteed. This agreement was made for Gay's benefit. Broder submitted a bill for \$95 which Gay paid. The Veterans Administration performed its agreement with Broder. Broder held himself out to be a qualified appraiser. He submitted an appraisal and negligently set the value of the property at \$85,000, although the reasonable value of the property was no less than the sales price of \$117,500. As a proximate result of this negligence, Gay was unable to obtain financing guaranteed by the Veterans Administration and was forced to obtain conventional financing, to his monetary damage.

There are tantalizing factors in this case that invite separate attention. For example, the veteran, Gay, paid the \$95 fee for the appraisal prepared by Broder ... why did the court hold no privity of contract existed? Again, what are the national policy that considerations that validate the concept that "the statute regulating Veterans Administration home loans ... was for the protection of the Veterans Administration rather than for that of a veteran seeking a Veterans Administration guaranteed home loan"?

These issues are tangential, however, to the present concern of the College: What is the best way to anticipate misunderstandings and disputations that, under the pitiless light of publicity, may force resolutions unacceptable to both parties and too often damaging to the "winner"? The *Gay v. Broder* lawsuit reflects at least one of the disadvantageous impacts of adversarial litigation: formal, published allegations of "negligence," "inaccurate appraisal," and "negligently set the value of the property" convey a permanent, damaging image to professional compeers and to the public. These are, unfortunately, hazardous by-products of adversarial litigation. There are alternatives, other than adversarial litigation, available to the professional practitioner. Two major alternatives: mediation and arbitration. Mediation, in general, places emphasis on direct problem-solving; responsibility and power for solutions remain with the parties involved, assisted by a third party trained in mediation techniques. Arbitration, in general, is also directly concerned with problem solving; however, decision-making authority is placed in the hands of the third-party mediator. Both of these alternatives avoid publicity; the proceedings can be employed with strict confidentiality.

Advantages of both procedures may include speed of settlement, relative inexpensiveness, and potential for achievement of solutions acceptable to both parties. From the perspective of the professional, however, the most important feature of mediation and arbitration is that of confidentiality. Confidentiality permits freedom from the haphazard pressures of publicity and the focused pressures of documented litigation and also provides a communications environment whereby reasoned discussion and objective negotiation may serve to reach solutions best suited to the long-range interests of the parties. In view of the unfavorable impacts that adversarial litigation may produce, it appears prudent for professional practitioners to employ dispute resolution procedures that have the greatest potential for avoiding publicity and lawsuit and that offer maximum emphasis upon problem-solving and negotiated settlement. To this end, the College recommends that alternative dispute resolution avenues, especially mediation and arbitration, be employed by appraisal practitioners and that the most effective means to ensure use of such media is through employment of a clause in the appraisal contract agreement that precedes commencement of the appraisal assignment. An appropriate clause has been suggested by the College in its 1990 Opinion on Contractual Conditions:

In the event of a dispute involving interpretation or application of this agreement, the dispute shall be referred to a neutral third-party mediation service. The cost of such mediation shall be borne equally by the parties. In the event mediation is not successful, the parties agree to submit the dispute to binding arbitration under the laws of the state of \_\_\_\_\_.

As expressed in the initial statements of this Opinion, the concern of the College is directed toward identification of measures that may be taken, by the appraiser and the appraisal society, to protect the reputation of practitioner, the client, and the profession. Certainly one such measure is the avoidance of lawsuit and the publicity surrounding a dispute between an appraiser and a client. Another measure is the provision for settlement of disputes through an effective medium, such as mediation/arbitration, that assures confidentiality. This concern must not, however, obscure the wider perspective contained in the society's Code of Ethics re the appraiser's fiduciary responsibility to clients and to third parties.

Our summary review of *Gay v. Broder* highlights a major factor in all professional practice: the practitioner works in a highly visible, public environment that is defined, ordered, and constrained by a variety of societal structures that operate within rigidly regulated patterns. We have viewed, in the lawsuit, a governmental organization that is described as operating within a regulatory network designed for the protection of itself rather than for that of its client. Additionally, we have reviewed the workings of "the law" as reflected in a formal account of a judicial proceeding in which no privity of contract, no fiduciary relationship to third parties, was permitted to be established.

In summary, the ethical responsibility of members of the American Society of Appraisers is greater than that represented by the regulations of governmental organizations indifferent to third-party relationships; it is greater than the minimal mandates of judicial rationale as voiced in the *Gay v. Broder* lawsuit. Practitioners who have accepted the criteria contained in the society's Code of Ethics must be aware of the nature and extent and responsibility of these maximum expectations. With such awareness, recognition of the need to protect their professional practice will encourage members to provide for the use of mediation/arbitration as appropriate instruments for achieving potential client dispute resolution. Such provision can be best achieved by inclusion of a mediation/arbitration clause in the appraisal contract agreement.