

August 18, 2003

Members of the Legislative Budget  
and Audit Committee:

In accordance with the provisions of Title 24 of the Alaska Statutes, the attached report is submitted for your review.

DEPARTMENT OF COMMUNITY AND  
ECONOMIC DEVELOPMENT  
BOARD OF CERTIFIED REAL ESTATE APPRAISERS  
SUNSET REVIEW

July 17, 2003

Audit Control Number

08-20024-03

This audit was conducted as required by AS 44.66.050 and under the authority of AS 24.20.271(1). Alaska Statute 44.66.050(c) lists criteria to be used to assess the demonstrated public need for a given board, commission, agency, or program subject to the sunset review process. Currently under AS 08.03.010(c)(20), the Board of Certified Real Estate Appraisers is scheduled to terminate on June 30, 2004. If the legislature takes no action to extend the termination date, the board would be allowed one year in which to conclude its administrative operations.

In our opinion, the termination date for the Board of Certified Real Estate Appraisers should be extended. The certification of appraisers remains a central requirement attached to various types of real estate loans made by federally insured financial institutions. We recommend the legislature extend the termination date of the Board of Certified Real Estate Appraisers to June 30, 2008.

This sunset review was conducted in accordance with generally accepted government auditing standards. Fieldwork procedures utilized in the course of developing this report are set out in the Objectives, Scope, and Methodology section.

Pat Davidson, CPA  
Legislative Auditor

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# OBJECTIVES, SCOPE, AND METHODOLOGY

In accordance with the intent of Titles 24 and 44 of the Alaska Statutes, we have reviewed the activities of the Board of Certified Real Estate Appraisers (BCREA) to determine if the termination date for the board should be extended. As required by AS 44.66.050(a), the legislative committee of reference shall consider this report as part of the oversight process in determining if BCREA should be reestablished. Currently, AS 08.03.010(c)(20) specifies that BCREA will terminate on June 30, 2004. If no action is taken by the legislature, the board will have one year from that date to conclude its administrative operations.

## Objectives

The three central, interrelated objectives of our report are:

1. To determine if the termination date of the board should be extended.
2. To determine if the board is operating in the public interest.
3. To determine if the board has exercised appropriate regulatory oversight of real estate appraisers.

The assessment of the operations and performance of the board was based on criteria set out in AS 44.66.050(c). Criteria set out in this statute relate to the determination of a demonstrated public need for the board.

## Scope and Methodology

Under the direction and supervision of the Division of Legislative Audit, another auditor conducted the majority of this review. We followed professional standards to determine that the other auditor was independent and that their work was competent and sufficient.

The major areas of our review were board proceedings, licensing, complaint investigation, and resolution functions. During the course of our examination we reviewed and evaluated the following:

- Applicable statutes and regulations.
- Files and documentation related to individuals certified as appraisers, including those who have been issued a courtesy license to practice within Alaska.
- Files and documentation related to individuals who applied for certification as an appraiser or for a courtesy license to practice within Alaska.

- Minutes of board meetings, budget documents, and annual reports related to, or issued by BCREA.
- Complaints filed with the Division of Occupational Licensing, the Alaska State Commission for Human Rights, the Office of the Ombudsman, the Office of Victims' Rights, and the Federal Equal Employment Opportunity Commission.
- Correspondence with the Appraisal Subcommittee, a national organization that reviews the regulation and oversight of real estate appraisers.
- A report to Congress by the U.S. General Accounting Office that assessed the oversight of real estate appraisers.

Additionally, we conducted interviews with Division of Occupational Licensing staff.

## ORGANIZATION AND FUNCTION

Alaska Statute 08.87.010 establishes the Board of Certified Real Estate Appraisers (BCREA). BCREA consists of five members, specified in statute to consist of at least one each of the following: (1) a certified general real estate appraiser, (2) a certified residential real estate appraiser, (3) a mortgage banking executive, and (4) a person from the general public. The fifth board position is undesignated in statute, and is commonly referred to as the “at large” position. Currently, the member at large happens to also be a certified general real estate appraiser.

Alaska Statute 08.87.020 defines the board’s authority, purpose, and scope of work. Under this statute BCREA establishes the following: (1) examination specifications for certification as a real estate appraiser; (2) rules of professional conduct to establish and maintain a high standard of integrity in the real estate appraisal profession; and, (3) regulations necessary to carry out the purposes of the statutes.

**BOARD OF CERTIFIED REAL ESTATE APPRAISERS**  
*(As of June 30, 2003)*

**Stephen Turner, Residential Real Estate Appraiser**  
*—Vice Chair (no Chair as of above date)*

**James A. Hage, Member at Large**

**Nelida Irvine, Public Member**

**Judy Kemplen, Mortgage Banking Executive**

**Steven J. MacSwain, MAI, General Real Estate Appraiser**

BCREA certifies general real estate appraisers, residential real estate appraisers, institutional appraisers,<sup>1</sup> and registers appraiser trainees. Courtesy licenses are also issued for real estate appraisers who are certified or licensed in other states but are temporarily practicing in Alaska.

Qualifications for certification as a general and residential real estate appraiser include education related to real estate appraisal, experience in real property appraisal, and passing an examination endorsed by the board. The qualifications for receiving an institutional appraisal certificate are that the applicant is a full-time employee of a financial institution with offices in Alaska, and the applicant meets education and testing requirements. The requirement to become a registered trainee includes 75 hours of instruction in courses related to real estate appraisal theory or practices from an organization approved by the board.

Real estate appraisal certificates are renewed biennially. The next biennial renewal date is June 30, 2005. In order to renew their certification, certified appraisers must complete a renewal application, provide evidence of continuing education, and remit a license fee. Individuals certified or licensed as appraisers in other jurisdictions can obtain a courtesy license to conduct appraisals in Alaska. Such licenses are issued for a single appraisal assignment, and individuals are limited to only one courtesy license every twelve months.

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<sup>1</sup> While BCREA has the authority to certify institutional appraisers, as of the date of this report, no individuals have applied for this certification.

## Duties of the Department of Community and Economic Development

The Department of Community and Economic Development, Division of Occupational Licensing provides administrative and investigative assistance to BCREA. This includes budgetary services and functions such as: collecting fees, maintaining files, receiving and issuing application forms, and publishing notice of examinations and meetings.

Alaska Statute 08.01.065 mandates the Department of Community and Economic Development, with the concurrence of the board, adopt regulations to establish the amount and manner of payment of application fees, examination fees, license fees, registration fees, permit fees, investigation fees, and all other fees as appropriate for the occupations covered by the statute.

Alaska Statute 08.01.087 empowers the Division of Occupational Licensing with the authority to act on its own initiative or in response to a complaint. The division may:

1. Conduct an investigation if it appears a person is engaged in, or is about to engage in, a prohibited professional practice.
2. Bring an action in superior court to enjoin the act.
3. Examine the books and records of an individual.
4. Issue subpoenas for the attendance of witnesses and records.

## **BACKGROUND INFORMATION**

An appraisal is a decision-making tool used to facilitate a real estate transaction. The primary role of appraisals in the loan underwriting process is to provide evidence that the collateral value of the property is sufficient to avoid losses on loans if the borrower was unable to repay the loan. Consumers often mistakenly assume that appraisals are intended to validate the purchase price of the property in question. In a loan transaction, the lender rather than the borrower engages the appraiser and this usually occurs after the borrower has agreed to purchase the property. The primary intent of federal statutory appraisal reforms was to protect the federal deposit insurance funds – and, by extension, mortgage lenders – from avoidable losses.

In 1986, the House Committee on Government Operations issued a report concluding that faulty and fraudulent appraisals contributed significantly to the losses that the federal government suffered during the savings and loan “crisis.”<sup>2</sup> In response to the “crisis,” Congress passed the 1989 Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA). Congress set out provisions in Title XI of FIRREA that were intended to ensure federally-related transactions had appraisals that were: (1) performed by real estate appraisers who met minimum qualifications criteria; and, (2) conducted in compliance with uniform standards.<sup>3</sup>

Title XI established a complex oversight structure for real estate appraisals and appraisers that involves private, federal, and state entities (see table, below).

<b>TITLE IX REGULATORY OVERSIGHT STRUCTURE AND ENTITIES</b>		
<b>PRIVATE</b>	<b>FEDERAL</b>	<b>STATE OF ALASKA</b>
<div style="border: 1px solid black; padding: 5px; margin-bottom: 5px; text-align: center;"><b>Appraisal Foundation</b></div> <ul style="list-style-type: none"> <li>▶ Appraisal Standards Board</li> <li>▶ Appraisal Qualifications Board</li> </ul>	<div style="border: 1px solid black; padding: 5px; margin-bottom: 5px; text-align: center;"><b>Appraisal Subcommittee</b></div> <div style="border: 1px solid black; padding: 5px; text-align: center;"> <p><b>Federal Financial Regulators</b></p> <ul style="list-style-type: none"> <li>▶ Federal Reserve System</li> <li>▶ Federal Deposit Insurance Corporation</li> <li>▶ Office of the Comptroller of the Currency</li> <li>▶ Office of Thrift Supervision</li> <li>▶ National Credit Union Administration</li> </ul> </div>	<div style="border: 1px solid black; padding: 5px; text-align: center;"> <p><b>Board of Certified Real Estate Appraisers</b></p> </div>

<sup>2</sup> *Impact of Appraisal Problems on Real Estate Lending, Mortgage Insurance, and Investment in the Secondary Market*, H.Rep. 99–891 at 4–6 (Sept. 25, 1986), House Committee on Government Operations, 99th Congress, 2nd session.

<sup>3</sup> U.S. Code 3331 - 3351, Title XI, Financial Institutions Reform, Recovery, and Enforcement Act of 1989.

## Appraisal Foundation

The Appraisal Foundation, a nonprofit educational organization composed of groups from the real estate industry, provides the organizational framework for the Appraisal Standards Board (ASB) and the Appraiser Qualifications Board (AQB) to carry out their responsibilities related to Title XI.<sup>4</sup> The Appraisal Foundation was founded in 1987 by eight leading professional appraisal organizations in the United States to foster professionalism in real estate appraising. ASB and AQB establish minimum standards for developing and reporting an appraisal and the minimum criteria for certified appraisers in connection with federally related transactions.

ASB is responsible for setting standards for appraisals and is composed of six appraisers who are appointed for three-year terms by the Board of Trustees of the Appraisal Foundation. ASB's minimum standards for appraisals are contained in the Uniform Standards of Professional Appraisal Practice (USPAP). Under Title XI, these minimum standards apply to all federally-related transactions. The standards cover both of the steps appraisers must take in developing appraisals and information the appraisal report must contain.

AQB is composed of five appraisers who are appointed for three-year terms by the Board of Trustees of the Appraisal Foundation, establishes the minimum education, experience, and examination requirements for state-certified real estate appraisers (set out in Real Property Appraiser Qualification Criteria and Interpretations of the Criteria). In addition, AQB performs a number of ancillary duties related to real property and personal property appraiser qualifications. The AQB's criteria covers four categories of appraisers—certified general, certified residential, licensed, and trainee—each with specific education, experience, examination, and continuing education requirements.

## Appraisal Subcommittee

The Appraisal Subcommittee (ASC) was established by U.S. law as the principal federal agency responsible for monitoring the activities of the other components of the real estate appraisal industry oversight structure. Specifically, ASC is responsible for:

- Monitoring and reviewing the practices, procedures, activities, and organizational structure of the Appraisal Foundation—including making grants in amounts that it deems appropriate to the Appraisal Foundation to help defray costs associated with its Title XI activities;

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<sup>4</sup> The 2002 sponsors of the Appraisal Foundation consisted of eight appraisal organizations, four affiliate organizations (representing primarily the users of appraisal services), and one international appraisal organization. In addition, over 80 organizations, corporations, and government agencies are affiliated with the Appraisal Foundation.

- Monitoring the requirements established by the states, territories, and the District of Columbia and their appraiser regulatory agencies for the certification and licensing of appraisers;
- Monitoring the requirements established by the federal financial institution regulators regarding appraisal standards for federally related transactions and determinations of which federally-related transactions will require the services of state-licensed or state-certified appraisers;
- Maintaining a national registry of state-licensed and state-certified appraisers who may perform appraisals in connection with federally-related transactions; and,
- Transmitting an annual report to Congress regarding the activities of ASC during the preceding year.

ASC has six board members and seven staff members. Each of the respective board members is designated by the head of the Department of Housing and Urban Development's Federal Housing Administration (HUD/FHA) and the heads of the following five financial institution regulatory agencies:

1. Board of Governors of the Federal Reserve System,
2. Federal Deposit Insurance Corporation,
3. Office of the Comptroller of the Currency,
4. Office of Thrift Supervision, and
5. National Credit Union Administration.

#### State Oversight—Board of Certified Real Estate Appraisers

States may establish, under Title XI, their own agencies to certify and license appraisers. In 1990, the Alaska State Legislature created the Board of Certified Real Estate Appraisers (BCREA) in response to FIRREA. Although BCREA is responsible for the certification of appraisers, ASC has a role in ensuring Alaska's qualifications satisfy Title XI objectives. Federal agencies and federal financial institutions may not accept appraisals from BCREA certified appraisers if the subcommittee issues a written finding that:

- a. BCREA has failed to recognize and enforce the standards, requirements, and procedures of Title XI;
- b. BCREA does not have enough authority to carry out its functions under Title XI; or,

- c. BCREA does not make decisions on appraisal standards and qualifications or supervise appraiser practices in a method that carries out the purposes of Title XI<sup>5</sup>.

In addition, BCREA is required to provide ASC with the names of those appraisers who become certified or licensed in accordance with Title XI and to collect from them an annual registry fee that goes to the subcommittee.

In August 2001, BCREA was the subject of an ASC review. ASC found all but one of the eight earlier review findings had been appropriately resolved by the board.<sup>6</sup> In their report, ASC commented that “*Alaska needs to revise its [Courtesy License] regulations to comply with Title XI of [FIRREA]...*” In addition, ASC developed two new findings that required action by the board. The board is proposing regulatory and procedural changes to implement all ASC recommendations made in the 2001 report.

Recent federal study determined oversight of real estate appraisers should be enhanced.

In May 2003, the U.S. General Accounting Office (GAO) issued a report regarding oversight of the real estate appraisal industry. The primary policy question addressed in the report was whether certain provisions of FIRREA that require certification of real estate appraisers are still necessary.

GAO was asked to conduct this review because some industry observers believed the appraisal industry regulations, required by FIRREA, are no longer needed.<sup>7</sup> Others argued that the law’s purpose and scope should be expanded.

In the report,<sup>8</sup> GAO concluded there was not only a continuing need for appraisers to be certified and regulated at the state level, but federal regulatory oversight should be enhanced. Among other things, GAO recommended that ASC “*develop and apply consistent criteria for determining and reporting states’ compliance levels with Title XI.*” GAO also recommended that ASC “*explore potential options for assisting states in carrying out their [regulatory oversight] activities, particularly for investigating appraiser complaints.*”

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<sup>5</sup> 12 USC § 3347(a), (b) (2000).

<sup>6</sup> BCREA is subject to ASC reviews on a triennial basis. Prior to the 2001 review, the most recent ASC review was conducted in August 1998.

<sup>7</sup> More specifically, the report commented that some observers believed both “*the risk to federal deposit insurance funds and the lack of uniform [appraisal] standards and [appraiser] qualifications*” no longer existed.

<sup>8</sup> An abridged version of the GAO report is included as Appendix A to this report beginning on page 19. A complete report can be found at [www.gao.gov/cgi-bin/getrpt?GAO-03-404](http://www.gao.gov/cgi-bin/getrpt?GAO-03-404).

## REPORT CONCLUSIONS

In accordance with AS 08.03.010(c)(20), the Board of Certified Real Estate Appraisers (BCREA) is presently scheduled for termination on June 30, 2004. If no action is taken by the legislature, the board has one year in which to conclude its affairs and will be dissolved at June 30, 2005.

The BCREA has been given the responsibility in AS 08.87.020 to: *(1) establish the examination specifications for certification as a general real estate appraiser, as a residential real estate appraiser, and as an institutional appraiser; (2) adopt rules of professional conduct to establish and maintain a high standard of integrity in the profession; and, (3) adopt regulations necessary to carry out the purpose of [the appraiser statute]...* As discussed in the Background Information section, a recent GAO study concluded that, nationwide, there is an ongoing need not only to maintain, but also to enhance these oversight functions.

The use of state certified real estate appraisers will be a continuing requirement for Alaska's financial institutions to qualify for federal deposit insurance and to participate in selling mortgage loans to federal government-sponsored enterprises.<sup>9</sup> Failure to maintain a real estate appraiser certification program that meets federal requirements could cause the financial institutions – and by extension, the citizens – of the State to not only lose the opportunity to participate in a number of federally-sponsored real estate loan programs, but also the ability to obtain federal deposit insurance. In this context, we recommend that the legislature extend BCREA's termination date to June 30, 2008.

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<sup>9</sup> Government-sponsored enterprises include such entities as the Federal Home Loan Mortgage Corporation (generally referred to as "Freddie Mac") and the Federal National Mortgage Association (generally referred to as "Fannie Mae").

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## **A****NALYSIS OF PUBLIC NEED****D**

The following analyses of board activities relate to the public need factors defined in AS 44.66.050(c). These analyses are not intended to be comprehensive, but address those areas we were unable to cover within the scope of our review.

***The extent to which the board, commission, or program has operated in the public interest.***

As reflected in the discussion under the Background Information section, the original impetus for establishing the Board of Certified Real Estate Appraisers (BCREA) was the federal law passed by Congress responding to the savings and loan “crisis” of the 1980s. Accordingly, most of the regulatory and statutory requirements that BCREA responds to is set by organizations and entities established by, or affiliated with, the federal government.

As part of that federal oversight, the board’s regulations and activities are periodically reviewed by the Appraisal Subcommittee (ASC) of the Federal Financial Institutions Examination Council.

In August 2001, BCREA was the subject of an ASC review. ASC found all but one of the eight earlier review findings had been appropriately resolved by the board.<sup>10</sup> In their report, ASC commented that “*Alaska needs to revise its [Courtesy License] regulations to comply with Title XI of Financial Institutions Reform, Recovery, and Enforcement Act [FIRREA]...*” In addition, ASC developed two new findings that required action by the board. The board is proposing regulatory and procedural changes to implement all ASC recommendations made in the 2001 report.

***The extent to which the operation of the board, commission, or agency program has been impeded or enhanced by existing statutes, procedures, and practices that it has adopted, and any other matter, including budgetary, resource, and personnel matters.***

Most of the board’s revenue is from certification, licensing, and renewal fees. Renewals are conducted on a biennial basis. This creates a two-year cycle in the board’s revenues, with the board receiving most of its revenues during the renewal period. We reviewed the internal records maintained by the Occupational Licensing (OccLic) for revenues and expenditures associated with the Board of Certified Real Estate Appraisers. We did not audit this information, but present it on the following page for general information purposes.

AS 08.01.065(c) requires “...*that the total amount of fees collected for an occupation approximately equals the actual regulatory costs for the occupation.*” As the schedule on the

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<sup>10</sup> BCREA is subject to ASC reviews on a triennial basis. Prior to the 2001 review, the most recent ASC review was conducted in August 1998.

following page reflects, the board was running a substantial deficit at the end of FY 02. However, for the FY 03/04 biennial licensing period, license renewal fees were increased more than 45% – from \$515 to \$750. Additionally, board expenses for FY 03 are projected to decrease from the previous fiscal year.

<p style="text-align: center;"><b>State of Alaska</b>  <b>Board of Certified Real Estate Appraisers</b>  <b>Schedule of License Revenues and Board Expenditures</b>  <b>FY 99 - FY 02</b>  <b>(Unaudited)</b></p>				
	<u>FY 02</u>	<u>FY 01</u>	<u>FY 00</u>	<u>FY 99</u>
Revenue	\$ 18,676	\$ 77,645	\$ 8,680	\$ 77,355
Direct Expenses				
Personal Services	26,653	27,258	20,757	24,652
Travel	4,408	920	2,769	3,397
Contractual	23,227	17,339	7,881	13,943
Supplies	131	30	78	165
Equipment	-	-	-	-
Total Expenses	<u>54,419</u>	<u>45,547</u>	<u>31,485</u>	<u>42,157</u>
Indirect Expense	<u>6,281</u>	<u>7,423</u>	<u>7,207</u>	<u>7,044</u>
Total Expenses	<u>60,700</u>	<u>52,970</u>	<u>38,692</u>	<u>49,201</u>
Annual Surplus (Deficit)	<u>(42,024)</u>	<u>24,675</u>	<u>(30,012)</u>	<u>28,154</u>
Beginning Cumulative Surplus (Deficit)	9,690	(14,985)	14,954	(13,200)
Unallocated Administrative Indirect Revenue	<u>20</u>	<u>-</u>	<u>73</u>	<u>-</u>
Ending Cumulative Surplus (Deficit)	<u>\$ (32,314)</u>	<u>\$ 9,690</u>	<u>\$ (14,985)</u>	<u>\$ 14,954</u>

***The extent to which the board, commission, or agency has recommended statutory changes that are generally of benefit to the public interest.***

As discussed previously, during August 2001 the board was reviewed by the Appraisal Subcommittee (ASC) of the Federal Financial Institutions Examination Council. ASC presented BCREA with a list of recommendations which the board is implementing through various proposed regulatory and procedural changes.

These changes include clarifying the board's policy regarding the definition of "assignment" for courtesy license purposes, increasing the number of courtesy licenses a person may be issued within a year (from one to two per year), and lowering the fees charged for courtesy licenses, which ASC considered excessive. ASC also requested that BCREA require experience logs from certified residential real estate applicants, just as it does for certified general real estate applicants. Once implemented, these changes will bring Alaska regulations into compliance with Title XI of FIRREA.

As a result of one lengthy investigation, the board has sought to define moral turpitude in the regulation. BCREA recommended other statutory and regulatory changes primarily related to work experience, education requirements, and certification and renewal fees.

***The extent to which the board, commission, or agency has encouraged interested persons to report to it concerning the effect of its regulations and decisions on the effectiveness of service, economy of service, and availability of service that it has provided.***

The public received notice of all meetings consistent with the requirements of statute and regulation. The agenda of items to be discussed was available before scheduled meetings. A public comment period has been set aside in the agenda for each board meeting.

Interested parties can attend meetings in person or by teleconference. In addition to accepting public comment at the meetings, the board regularly discussed correspondence from various individuals, agencies and other interested parties. OccLic forwards public comment and concerns to the board for consideration during board meetings.

***The extent to which the board, commission, or agency has encouraged public participation in the making of its regulations and decisions.***

Draft regulations developed by the board were properly advertised for the required amount of time. Public notices of regulatory hearings were published in major newspapers and on the board's website. The board accepted public comment at meetings. We found no indication in the BCREA records that public testimony has been inappropriately restricted by the board.

***The efficiency with which public inquiries or complaints regarding the activities of the board, commission, or agency filed with it, with the department to which a board or commission is administratively assigned, or with the office of victims' rights or the office of the ombudsman have been processed and resolved.***

During the 48-month period from July 1, 1999 through June 30, 2003, the Division of Occupational Licensing opened 21 investigative cases related to individuals certified by the board. Almost half of the cases (9) involved complaints made by clients or individuals from the general public. Most of the complaints (15) involved alleged incompetence or professional ethics violations by the appraisers.

Of the 17 cases closed as of the date of our review, two resulted in licensure action involving the voluntary surrender of the appraiser's certificate. Of the remaining cases, 12 were closed with a finding of no violation, two were closed with warning letters issued by the board, while one case was closed through a referral to other investigative agencies (the Alaska Department of Labor and Workforce Development and the Internal Revenue Service).

Of the four cases not closed as of the date of our review, three had been opened within the previous 120 days. Of the three opened cases, two are in the process of closure and one is awaiting expert review by a board member. The remaining open case was still under active investigation and was being reviewed by the Department of Law.

We have reviewed the nature and extent of complaints filed involving appraisers. In our view OccLic, in conjunction with the board, has proceeded in a manner consistent with the potential threat the complaints posed to the public welfare.

There were no complaints filed with the Office of the Ombudsman or the Office of Victims' Rights for the period under review.

***The extent to which a board or commission that regulates entry into an occupation or profession has presented qualified applicants to serve the public.***

From FY 00 through FY 02 the board approved and certified 32 new appraisers and issued 35 courtesy licenses. We found no instances where the board issued a certificate or license to an unqualified candidate, nor did we find any instances where a qualified candidate was denied certification or licensure. The table below summarizes licensing activity for the prior three fiscal years, listing the number of new certificates or licenses issued each year for each certificate or license type, as well as the number of current certificates.

<b>New Certificates Issued</b>	<b>FY 00</b>	<b>FY 01</b>	<b>FY 02</b>	<b>Total</b>	<b>Current Certificates as of June 30, 2002</b>
General Appraisers	0	4	0	4	70
Residential Appraisers	6	4	7	17	81
Institutional Appraisers	0	0	0	0	0
Total	6	8	7	21	151
Registered Appraiser Trainees	6	1	4	11	9
Courtesy Licenses Issued	13	12	10	35	--

***The extent to which state personnel practices, including affirmative action requirements, have been complied with by the board, commission, or agency to its own activities and the area of activity or interest.***

We found no evidence of the board not complying with state personnel practices, including affirmative action, in the qualifying process of applicants. Each time the board has denied an applicant's certification, reasoning has been based on requirements set out by statute and regulation, not on the personal attributes of applicants. The reasons for denials are stated in writing, with the applicant always informed of their rights and the process in which they can contest or appeal any denial of licensure.

***The extent to which statutory, regulatory, budgeting, or other changes are necessary to enable the agency, board, or commission to better serve the interest of the public and to comply with the factors enumerated in AS 44.66.050.***

As noted, much of the impetus and oversight of BCREA stems from actions taken by oversight organizations and entities affiliated with the federal government. In recent years, BCREA's licensing fees have not been set at a sufficiently high-enough level to cover the board's costs. However, as noted earlier in this section, the board has adopted a 45% increase in appraiser certification renewal fees and appears to have decreased board expenses.

During our review of the board's composition, we noted AS 08.87.010 requires two of the board members to be "licensed" real estate appraisers in the State of Alaska.

In the statutes, real estate appraisers are referred to as being certified, but state law does not use the term licensed. We encourage the department, when proposing sunset extension legislation, to consider amending AS 08.87.010 and make the nomenclature consistent within the statute.

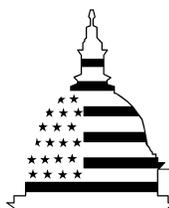
## APPENDIX A

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May 2003

REGULATORY  
PROGRAMS

Opportunities to  
Enhance Oversight of  
the Real Estate  
Appraisal Industry



G A O

Accountability \* Integrity \* Reliability

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Highlights of [GAO-03-404](#), a report to Congressional Requesters

# REGULATORY PROGRAMS

## Opportunities to Enhance Oversight of the Real Estate Appraisal Industry

### Why GAO Did This Study

Since the passage of Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, the appraisal and mortgage lending industry has changed dramatically. Some have concluded that the law is obsolete because the problems Title XI was intended to address—the risk to federal deposit insurance funds and the lack of uniform standards and qualifications—no longer exist. Others argue that the law’s purpose and scope should be expanded. To help Congress better understand these issues, GAO looked at the roles of the private, state, and federal entities that oversee the appraisal industry, the challenges Title XI presented to these entities, and industry participants’ concerns about the effectiveness of the Title XI regulatory structure.

### What GAO Recommends

Among other things, the Chairman of the Appraisal Subcommittee should:

- develop and apply consistent criteria for determining and reporting states’ compliance levels with Title XI;
- explore potential options for assisting states in carrying out their Title XI activities, particularly for investigating appraiser complaints; and
- explore alternatives for providing future Title XI grant funding to the Appraisal Foundation and its two boards.

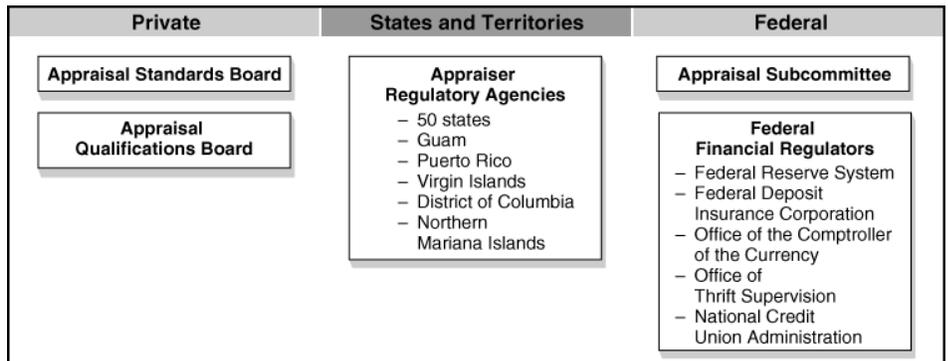
### What GAO Found

Title XI created a complex oversight structure for real estate appraisals and appraisers that involves private, state, and federal entities. Two private entities establish uniform rules for real estate appraisals and set minimum criteria for certifying appraisers. State regulatory agencies certify appraisers based on these criteria. The federal financial regulators oversee financial institutions’ use of appraisals, and a federal agency, the Appraisal Subcommittee, monitors and coordinates the functions of the parties involved in regulating appraisals and appraisers.

All of these entities except the federal financial regulators identified potential impediments to carrying out their Title XI responsibilities. The two private entities stated that fund limitations could impede their ability to ensure that development of standards and qualifications evolve with changing conditions. State agencies said that funding shortfalls hindered their ability to enforce compliance. Appraisal Subcommittee staff reported that rule-making authority and additional enforcement sanctions could facilitate its oversight of state compliance with Title XI.

Industry participants raised concerns about aspects of the Title XI regulatory system for appraisers. They cited differences in state regulation that affect both lenders and appraisers, gaps in Title XI’s coverage—for example, transactions of less than \$250,000 do not require an appraisal—high fees and burdensome processes for having appraiser education courses approved, and weak enforcement and complaints processing. Some industry participants felt that states, traditionally involved in regulating professions, alone should regulate the appraisal industry. Others felt that the current structure needed a significant overhaul to become effective.

**Title XI Regulatory Oversight Structure and Entities**



Source: GAO.

[www.gao.gov/cgi-bin/getrpt?GAO-03-404](http://www.gao.gov/cgi-bin/getrpt?GAO-03-404).

To view the full report, including the scope and methodology, click on the link above. For more information, contact David G. Wood (202) 512-8678 or [woodd@gao.gov](mailto:woodd@gao.gov).



United States General Accounting Office  
Washington, D.C. 20548

May 14, 2003

The Honorable Paul S. Sarbanes  
Ranking Minority Member  
Senate Committee on Banking,  
Housing, and Urban Affairs  
United States Senate

The Honorable Zell Miller  
United States Senate

Recent predatory mortgage lending cases, involving fraudulent and inflated appraisals, have highlighted the need for accurate real estate appraisals in preventing losses to the federal government and significant financial harm to individual consumers. When making mortgage loans, lenders need an objective and accurate assessment of the value of properties used as collateral to help avoid losses in the event that borrowers do not repay the loans. Congress enacted Title XI of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) in response to concerns that faulty and fraudulent appraisals played a major role in the savings and loans crisis of the 1980s. Title XI provisions address both the quality of *appraisals* and the qualifications of *appraisers*. Specifically, Title XI requires that real estate appraisals used in connection with federally related transactions be performed (1) in writing, in accordance with uniform professional standards, and (2) by individuals whose competency has been demonstrated and whose professional conduct is subject to effective supervision.<sup>1</sup>

To ensure that the purpose of the legislation was carried out, Title XI created a regulatory structure to monitor and oversee the real estate appraisal industry. Among other things, it established a federal entity called the Appraisal Subcommittee to monitor the Title's implementation. Title XI provides for national uniformity in appraisal standards and minimal national qualification requirements for some, but not all, appraisers. The Title XI regulatory structure was set up primarily to protect federally

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<sup>1</sup>As defined in Title XI, federally related transactions are real estate transactions involving financial institutions regulated by the federal government. These include banks, thrifts, and credit unions. Real estate transactions of mortgage bankers, brokers, pension funds, and insurance companies are not included.

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insured depository institutions from losses and by extension the federal deposit insurance funds.

Because of your concerns about the effectiveness of the current regulatory structure, you requested that we assess the appraisal oversight structure established in response to Title XI. As agreed with your offices, this report describes (1) the specific responsibilities under Title XI of the private, state, and federal entities that oversee the appraisal industry and the way these entities perform their roles; (2) factors that these entities identified as potential impediments to carrying out their Title XI responsibilities; and (3) concerns expressed by regulatory entities and industry participants about the effectiveness of the existing regulatory structure.

To answer these questions, we reviewed FIRREA and its legislative history; interviewed representatives of the private, state, and federal entities involved in the Title XI regulatory scheme; and, using a mailed questionnaire, surveyed appraiser regulatory agencies in the 50 states, the District of Columbia, and 4 U.S. territories.<sup>2</sup> A copy of the questionnaire, including summary responses to each question, can be found in appendix I. Additionally, we contacted industry participants, including trade groups that represent appraisers and lenders; Fannie Mae and Freddie Mac, two government-sponsored enterprises (GSE) that establish standards for appraisals used in connection with mortgages that they purchase; the Department of Housing and Urban Development (HUD), which establishes requirements for appraisals used in connection with mortgages it insures; representatives of appraiser education providers; and academic experts on issues related to real estate appraisals. We also obtained and reviewed records of the Appraisal Subcommittee's state oversight activities, as well as information on appraisers maintained in the subcommittee's national registry database. We conducted our work between March 2002 and March 2003 in accordance with generally accepted government auditing standards. Appendix II provides a detailed discussion of our scope and methodology, and appendix III contains a list of the entities that we contacted.

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<sup>2</sup>The territories included in our survey are Guam, Northern Mariana Islands, Puerto Rico, and the Virgin Islands. The only other U.S. territory—American Samoa—does not have a regulatory oversight structure for appraisers because real estate there can only be inherited. In this report, the term “states and territories” refers to the 50 states, the District of Columbia, and the 4 territories.

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## Results in Brief

Title XI created a complex regulatory system that relies upon the actions of private, state, and federal entities to help assure the quality of appraisals and the qualifications of appraisers used in federally related transactions.

- The two private entities—the Appraisal Standards Board and Appraiser Qualifications Board—respectively establish (1) uniform rules for preparing and reporting real estate appraisals and (2) minimum qualification criteria for certified real estate appraisers. Certified real estate appraisers are one of the two categories of appraisers listed in Title XI, the other being licensed real estate appraisers.
- Title XI defers to the states with respect to the minimum qualification criteria for the licensed appraisers. In addition, Title XI relies on the states to (1) implement the certification and licensing of all real estate appraisers and (2) monitor and supervise compliance with appraisal standards and requirements. To assure the availability of certified and licensed appraisers, all of the states and territories have adopted structures to regulate and supervise the appraisal industry. These structures typically consist of a state regulatory agency coupled with a board or commission to establish education and experience requirements, license and certify appraisers, and monitor and enforce appraiser compliance.
- The federal financial institution regulators—defined in Title XI as the Federal Reserve System (FRS), Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), Office of Thrift Supervision (OTS), and National Credit Union Administration (NCUA)—are responsible for ensuring that federally insured depository institutions comply with Title XI requirements. To meet these responsibilities, the regulators have (1) adopted rules and policies specifying transactions for which regulated financial institutions are required to obtain an appraisal by a certified or licensed appraiser, (2) developed examination procedures to ensure that regulated financial institutions are in compliance with Title XI, and (3) appointed agency representatives to the Appraisal Subcommittee.
- The Appraisal Subcommittee is responsible for monitoring the implementation of Title XI by all parties—private, state, and federal. The subcommittee monitors the efforts of the federal financial institution regulators in developing and adopting appraisal-related regulations and policies, conducts periodic reviews of each state’s licensing and

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certification program, and provides grants to the Appraisal Foundation to support the Title XI-related activities of its two boards—Appraisal Standards Board and Appraiser Qualifications Board.

The private, state, and federal entities involved in the Title XI regulatory structure described a number of factors that they believe could constrain their ability to perform more effectively and efficiently. For example, officials of the Appraisal Standards Board and the Appraiser Qualifications Board told us that insufficient federal grant funding may impede their ability in the future to ensure that standards and qualifications evolve with changing conditions, such as how to appraise contaminated or polluted properties. State appraiser agencies—which are funded at the state level—reported resource limitations as the primary impediment in carrying out their oversight responsibilities. For example, of the 54 states and territories that responded to our survey, 26 reported that the current number of investigators was insufficient for meeting its regulatory responsibilities, 37 cited a need for increasing the staff directed at investigations, and 22 cited a need for more resources to support litigation. Officials of the five federal financial institution regulators reported no major impediments to accomplishing their Title XI responsibilities. The Appraisal Subcommittee reported that rule-making authority and additional enforcement sanctions could facilitate its oversight of state compliance with Title XI. Subcommittee officials stated that the only enforcement action they can take under Title XI is to decertify a state, which would prohibit all licensed or certified appraisers from that state from performing appraisals in conjunction with federally related transactions. Subcommittee officials stated that using this sanction would have a devastating effect on the real estate markets and financial institutions within the state. However, the Appraisal Subcommittee stated that it has always been able to achieve states' compliance under the current enforcement and regulatory structure.

In addition to the impediments described above, officials of the regulatory agencies, appraiser trade groups, education providers, mortgage industry, HUD, and the GSEs raised concerns about the Title XI regulatory structure. However, there was no clear consensus regarding the need for or impact of possible changes. Some industry participants stated that a growing number of real estate transactions, such as those placed through mortgage brokers and those involving dollar amounts below the threshold level established by the federal financial institution regulators, are not universally subject to Title XI appraisal requirements. In addition, some industry participants cited concerns with the lack of a national qualification standard for the licensed real estate appraiser category. Education providers and appraiser

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trade groups expressed concerns about the Appraiser Qualifications Board's fees and requirements for instructor certification and course approval. Federal and state regulatory officials expressed concern about the apparent reluctance of lending institutions to make referrals or complaints regarding questionable appraisals they identify. HUD and GSE officials expressed concerns about a lack of consistent and effective enforcement actions by the states on referred cases and the adequacy of the Appraisal Subcommittee's oversight of state programs. This report makes recommendations to the Appraisal Subcommittee intended to enhance the effectiveness of the existing regulatory structure.

We received written comments on a draft of this report from the Appraisal Subcommittee, the Appraisal Foundation, HUD, Fannie Mae, and Freddie Mac. In addition, we received technical comments from the federal financial institutions regulators, who indicated that their overall comments had been incorporated into those provided by the Appraisal Subcommittee. The Appraisal Subcommittee agreed to take action on our recommendation to develop and apply consistent criteria for determining and reporting states' compliance with Title XI, and did not comment on our recommendation for greater coordination with HUD, Fannie Mae, and Freddie Mac on referrals of problem appraisers. Concerning the remaining two recommendations, the Appraisal Subcommittee

- agreed that additional funding for the states would improve compliance with Title XI, but stated that the Subcommittee is not the answer to that issue. Because the recommendation is to explore additional funding as well as other options for assisting the states, we did not revise it.
- agreed that the Appraisal Foundation faces future grant funding constraints, but stated that using the Subcommittee's surplus is not a long-term solution. We modified the report to emphasize that we are recommending that the subcommittee explore options, including drawing on the subcommittee's surplus, if necessary, for addressing future Appraisal Foundation grant shortfalls.

HUD agreed with our recommendation for greater coordination on referrals of problem appraisers to state appraiser agencies. Both Fannie Mae and Freddie Mac expressed concern about this recommendation, commenting that they are not regulatory entities. We revised the wording of our recommendation to emphasize the role that HUD, Fannie Mae, and Freddie Mac can play in helping the subcommittee carry out its oversight responsibilities.

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## Background

An appraisal is a decision-making tool used to facilitate a real estate transaction. The primary role of appraisals in the loan underwriting process is to provide evidence that the collateral value of the property is sufficient to avoid losses on loans if the borrower was unable to repay the loan. Consumers often mistakenly assume that appraisals are intended to validate the purchase price of the property in question. Furthermore, appraisals are sometimes confused with home inspections, which are intended to warn consumers about serious defects in the home being purchased that should be repaired. In a loan transaction, the lender rather than the borrower engages the appraiser and this usually occurs after the borrower has agreed to purchase the property. The primary intent of the appraisal reforms contained in Title XI was to protect the federal deposit insurance funds—and, by extension, mortgage lenders—from avoidable losses.

An appraisal is an opinion of the value of a property as of a specific date. Appraisers generally consider the property's value from three points of view—cost, income, and comparable sales—and determine an estimated value based upon weighing the three valuation methods. The cost approach is based on an estimate of the value of the land plus what it would cost to replace or reproduce the improvements minus the physical deterioration, functional obsolescence, and economic obsolescence. The income approach is of primary importance in ascertaining the value of income producing properties and is an objective estimate of what a prudent investor would pay based upon the net income the property produces. The comparable sales approach compares and contrasts the property under appraisal with recent offerings and sales of similar property. This approach is usually considered the most appropriate valuation approach for estimating the value of residential real estate property.

In 1986, the House Committee on Government Operations issued a report concluding that faulty and fraudulent appraisals were an important contributor to the losses that the federal government suffered during the savings and loan crisis.<sup>3</sup> In response, Congress incorporated provisions in Title XI of FIRREA that were intended to ensure that federally related transactions had appraisals that were (1) performed by real estate

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<sup>3</sup>*Impact of Appraisal Problems on Real Estate Lending, Mortgage Insurance, and Investment in the Secondary Market*, H.Rep. 99-891 at 4-6 (Sept. 25, 1986), House Committee on Government Operations, 99th Congress, 2<sup>nd</sup> session.

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appraisers that had met minimum qualifications criteria and (2) conducted in compliance with uniform standards.

In addition to those identified in Title XI, there are other federal and government sponsored entities that have roles with respect to oversight of the real estate appraisal industry. Among these entities, the most important with respect to appraisal oversight issues are the HUD's Federal Housing Administration (HUD/FHA) and the two large GSEs that purchase residential loans in the secondary market—Fannie Mae and Freddie Mac. HUD/FHA uses appraisals to determine a property's eligibility for mortgage insurance and to estimate the value of a property for mortgage insurance purposes. Certified and licensed appraisers wishing to perform appraisals for HUD/FHA loans must first be placed on the FHA Roster of Appraisers, which requires the appraiser to pass a HUD/FHA examination on appraisal methods and meet other eligibility requirements. Both Fannie Mae and Freddie Mac consider appraisals or evaluations of the property value as a vital part of their risk analysis for loans that they purchase. For those loans for which Fannie Mae and Freddie Mac require an appraisal, the lender is required to use an appraiser that is state licensed or certified in accordance with the provisions of Title XI.<sup>4</sup> Fannie Mae and Freddie Mac largely hold the lender responsible for the selection and quality control of the appraiser. As such, Fannie Mae and Freddie Mac do not maintain a list of approved appraisers.

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## Title XI Created a Complex Appraiser Regulatory Oversight Structure

Various private, state, and federal entities play a role with respect to the Title XI regulatory structure (table 1). Private entities—the Appraisal Standards Board (ASB) and the Appraiser Qualifications Board (AQB)—establish minimum standards over the development and reporting of real estate appraisals and minimum qualification criteria for certified appraisers. States conduct the certification and licensing of appraisers, including setting education and experience requirements that, at minimum, must meet AQB criteria for certified appraisers and enforcing compliance with appraisal standards. FRS, FDIC, OCC, OTS, and NCUA—hereinafter referred to as the federal financial institution regulators—issue appraisal requirements for the financial institutions under their jurisdiction and

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<sup>4</sup>Both Fannie Mae and Freddie Mac allow lenders the options to use an inspection or evaluation instead of a traditional appraisal, on loans that they determine to be low-risk based on their automated loan underwriting systems. In the case of Freddie Mac, certain low risk loans may be eligible for delivery to Freddie Mac with no appraisal or inspection.

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monitor compliance with their regulations. Lastly, the Appraisal Subcommittee has primary responsibility for monitoring and reviewing the actions of the private, state, and federal entities as they relate to Title XI.

**Table 1: Title XI Roles and Responsibilities for Appraisal Standards and Appraiser Qualifications**

	Private	State	Federal	
Appraisal Standards Board (ASB)	Appraiser Qualifications Board (AQB)	Appraiser regulatory agencies	Financial institution regulatory agencies	Appraisal Subcommittee
<b>Appraisal standards</b>				
Standard setting				
Develop standards for the performance of real estate appraisals.			Promulgate regulations that establish appraisal standards, which meet or exceed ASB's standards, for federally insured depository institutions.	
Implementation/Monitoring				
		Enforce compliance with appraisal standards and requirements.	Monitor and enforce compliance by federally insured depository institutions with appraisal regulations.	<p>Monitor and review the Appraisal Foundation's practices, procedures, activities, and organizational structure.</p> <p>Monitor policies, practices, and procedures of states to determine consistency with Title XI requirements.</p> <p>Monitor appraisal requirements established by federal financial institution regulatory agencies.</p> <p>Make grants to the Appraisal Foundation to defray the costs of the Appraisal Standards Board's Title XI activities.</p>

(Continued From Previous Page)

	Private	State	Federal	
Appraisal Standards Board (ASB)	Appraiser Qualifications Board (AQB)	Appraiser regulatory agencies	Financial institution regulatory agencies	Appraisal Subcommittee
<b>Appraiser qualifications</b>				
Standard setting	Develop minimum qualification criteria for certified real estate appraisers.	Set qualifications criteria for certification, which meet or exceed AQB's criteria, and licensing of appraisers.	Establish additional qualification criteria as may be necessary or appropriate to carry out their statutory responsibilities.	
<b>Implementation/Monitoring</b>				
		Transmit to the Appraisal Subcommittee a roster of appraisers who have been licensed or certified.	Prescribe categories of federally related transactions that should be appraised by a state certified appraiser and those that can be performed by either a state certified or licensed appraiser.	Monitor qualification criteria set by states for the certification and licensing of individuals qualified to perform appraisals in connection with federally related transactions.
		Collect from appraisers and transmit to the Appraisal Subcommittee a \$25 annual registry fee.	Monitor and enforce compliance by federally insured depository institutions with appraisal regulations.	Maintain a national registry of state certified and licensed appraisers eligible to perform appraisals in federally related transactions.
		Enforce compliance with standards, requirements, and procedures prescribed by Title XI.		Monitor and review the Appraisal Foundation's practices, procedures, activities, and organizational structure.
				Make grants to the Appraisal Foundation to defray the costs of the Appraiser Qualifications Board's Title XI activities.

Source: GAO.

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October 3, 2003

Ms. Pat Davidson, Legislative Auditor  
Legislative Budget and Audit Committee  
Division of Legislative Audit  
P.O. Box 113300  
Juneau, AK 99811-3300

Dear Ms. Davidson,

Thank you for the opportunity to comment on your preliminary audit report on the Board of Certified Real Estate Appraisers.

The department concurs with the findings in your report. As you requested, I have also provided a summary of the Board's FY 03 revenues and expenditures.

Your report clearly identifies the background which led to creation of the licensing program for Real Estate Appraisers in Alaska, including oversight and standards mandated by the Appraisal Foundation, and the Appraisal Subcommittee. Title XI allow States to establish their own agencies to certify and license appraisers; and therefore, the Alaska State Legislature created the Board of Certified Real Estate Appraisers in 1990.

Generally, your findings indicate the licensing of Real Estate Appraisers are in compliance with federal mandates. Page 15 of the report states that license denials have been based on requirements set out by statute and regulation. Since creation of the Board and its current statutes and regulations, the licensing function has become perfunctory. The considerable amount of staff time required to prepare for board meetings and to provide administrative support to the Board actually slows down the licensing process. In the interest of providing better service to the public and potential licensees, I request consideration be given to elimination of the Board of Certified Real Estate Appraisers but, to continue licensing by the Division of Occupational Licensing.

Again, I appreciate the opportunity to comment on your findings.

Cordially,

Edgar Blatchford  
Commissioner

Enclosure

**State of Alaska**  
**Board of Certified Real Estate Appraisers**  
**Schedule of License Revenues and Board Expenditures**  
**FY 03**

Revenue	\$119,240
Direct Expenses	
Personal Services	20,011
Travel	1,005
Contractual	7,078
Supplies	195
Equipment	--
Total Expenses	<u>28,289</u>
Indirect Expense	<u>8,597</u>
Total Expenses	<u>36,886</u>
Annual Surplus (Deficit)	<u>82,354</u>
Beginning Cumulative Surplus (Deficit)	(32,314)
Unallocated Administrative Indirect Revenue	--
Ending Cumulative Surplus (Deficit)	<u>\$ 50,040</u>

Mr. Stephen F. Turner, Vice Chair  
Board of Certified Real Estate Appraisers  
P. O. Box 240088  
Anchorage, Alaska 99524-0088

September 9, 2003

Pat Davidson, CPA, Legislative Auditor  
Alaska State Legislature  
Legislative Budget and Audit Committee  
Division of Legislative Audit  
P. O. Box 113300  
Juneau, Alaska 99811-3300

Dear Ms. Davidson;

I have carefully reviewed the "CONFIDENTIAL" preliminary audit report on:

*Department of Community and Economic Development, Board of Certified  
Real Estate Appraisers, Sunset Review.*

I found the report to be thorough, both in its review of the historical context of the board, and in its assessment of the board's ongoing actions. The audit reaffirmed that we have appropriately handled our responsibilities and that we play an essential role in appraiser oversight.

I concur with the single recommendation that the wording of AS 08.87.010 be amended. As the audit points out, the law presently requires two of the board members to be "licensed" real estate appraisers in the State of Alaska. Since Alaska appraisers are certified, not licensed, the correct terminology should be "certified" real estate appraisers. I plan to bring this issue before the board at our next meeting with the intent that a motion be passed recommending this change.

Thank you for this opportunity to review and respond to the audit report. My responses, of course, are mine alone, and do not represent the entire board. Be assured that I understand that the report is confidential at this time, and is not for public release pending final review and approval by the Legislative Budget and Audit Committee.

Sincerely;



Stephen F. Turner, Vice Chair  
Board of Certified Real Estate Appraisers

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