



February 1, 2011

Employee Benefits Security Administration (EBSA)
U.S. Department of Labor
Room N-5655
200 Constitution Avenue, NW
Washington, DC 20210

Re: Attn: Definition of Fiduciary Proposed Rule (RIN 1210-AB32)

Dear Sir or Madam:

The undersigned professional appraisal organizations, representing thousands of professionally credentialed appraisers in the U.S. – many of whom provide ESOP-related valuation services – appreciate the opportunity to comment on the above-referenced proposed rule.¹ Our views are summarized and discussed below:

EXECUTIVE SUMMARY

A. In General

Although our organizations share EBSA's interest in strengthening the reliability and independence of ESOP-related valuations, we respectfully but strongly oppose the manner in which the proposed rule seeks to accomplish that objective. Including appraisers within ERISA's definition of "fiduciary" would impose unacceptable and unnecessary burdens both on appraisers and on the thousands of companies with ESOP plans. The "appraiser as fiduciary" approach of the proposed rule to improve the integrity of ESOP valuations is unproven and, we believe, otherwise ill-suited to accomplishing its intended purpose.

Importantly, if EBSA were to adopt the fiduciary approach to appraisal reform, its policy would be completely inconsistent with the appraisal reform policies of the many other federal agencies which administer appraisal programs or regulate private sector appraisal practice. When these agencies – including the Internal Revenue Service, the federal bank regulators, HUD/FHA and the government sponsored enterprises – found it necessary to bolster the reliability of their appraisal programs, each adopted a policy requiring that appraisals only be performed by individuals with professional appraisal designations who adhere to the Uniform Standards of Professional Appraisal Practice (USPAP) or to generally-accepted valuation standards that are consistent with the principles and purposes of USPAP. Moreover, this appraisal reform model

¹ Each of our organizations teaches, tests and credentials its members for professional appraisal practice and appraisal review in the area of commercial and residential real property valuation. Additionally, the American Society of Appraisers (ASA) is a multi-disciplinary appraisal organization that teaches, tests and credentials its members for professional appraisal practice and appraisal review in business valuation and in personal property valuation (including fine arts and machinery and technical specialties).

(i.e., reliance on professionally credentialed and fully accountable appraisers) was recently adopted by Congress when it enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act, to ensure the independence and integrity of valuations in federally-related financial transactions.

A strong consensus exists among those members of our organizations most experienced in performing ESOP valuations that adoption of the rule, as proposed, would produce two unintended and extremely negative consequences: First, it would necessitate a substantial increase in the cost of ESOP-related valuations – costs which would be passed through to companies with ESOP plans; and, Second, it would greatly reduce the numbers of professional appraisers willing to perform ESOP valuations because of the increased risk exposure. We are deeply concerned about the negative affects of the fiduciary rule on appraisers and on the ESOP program itself.

Accordingly, we respectfully urge EBSA, in connection with its efforts to improve the reliability and independence of ESOP valuations, to adopt the appraisal reform model that is being utilized successfully by other federal agencies with important valuation responsibilities – a model, as stated above, that was recently adopted by Congress in the Dodd-Frank financial reform and consumer protection law.

B. Reliance On Professionally Credentialed Appraisers For ESOP Valuations Would Address The Department’s Valuation Concerns In A Way That Is Both Proven and Cost-Effective

Congress and other federal agencies with important regulatory responsibilities for valuations have implemented the appraisal reform model we urge the Department to adopt for ESOP appraisals, because they recognize that professionally-credentialed appraisers are required to meet, at a minimum, the standards of independence, competence and accountability which the Department’s proposed rule seeks to establish through unproven means. They also recognize that the protocols of professional appraisal practice, including USPAP’s Ethics Rule, explicitly prohibit an appraiser from having any undisclosed financial or other economic interest in the property to be appraised or in the transaction giving rise to the appraisal. Professional appraisers who violate this anti-conflict-of-interest requirement are subject to a loss of their state-issued appraisal license (in the case of real estate appraisal practice) or of their professional appraiser credential issued by recognized professional appraisal organizations (in the case of designations awarded to business appraisers or to personal property appraisers).

In our judgment, expanding the definition of “fiduciary” to include appraisers would be a costly, unproven and ineffective way to ensure that ESOP appraisers are independent, competent and accountable.

C. The Seeds Of An Acceptable Alternative To The Proposed Rule Currently Exist In The Form Of EBSA's Appraisal Requirements For Prohibited Transaction Exemptions. With Minimal Changes, And By Extending Them To All ESOP Valuations, EBSA Appraisal Requirements Will Be Comparable To Those of Other Federal Agencies

While we are unable to support the rule as proposed, our organizations are very interested in working with EBSA to increase its confidence that ESOP-related appraisals are performed by professional appraisers with a high degree of competence, care and independence.

In this regard, we note that DOL's definitions of "Qualified Independent Appraiser" and "Qualified Appraisal Report" (in connection with Prohibited Transaction Exemption Procedures Under Federal Pension Laws) contain many of the general concepts included in the professional appraisal requirements of IRS and other federal agencies – but lack their specificity and the objective standards they establish. We also note, approvingly, that EBSA has proposed amendments to its exemption procedures which define with additional specificity requirements pertaining to what constitutes a "Qualified Independent Appraiser" and a "Qualified Appraisal Report".² While the proposed additional requirements are somewhat less detailed and objective than the appraisal reform systems at other federal agencies, they nevertheless provide a good basis for an appraisal reform system that addresses EBSA's valuation concerns. Of course, the Department's appraisal requirements pertaining to prohibited transaction exemptions would have to be extended to cover all ESOP-related appraisals. But, this is readily doable and would result in an EBSA appraisal reform system comparable to those at IRS and other federal agencies.

The existing appraisal procedures regarding prohibited transaction exemptions state that a "Qualified Independent Appraiser" "must represent in writing its qualifications to serve in that capacity.... and must demonstrate that he/she has experience in valuing assets of that type." However, the exemption procedures do not establish any objective standards regarding qualifications and experience. By contrast, IRS Guidance for valuations of tangible and intangible property for contributions of non-cash charitable contributions (and for other Income and Estate tax purposes) set forth specific and concrete requirements governing both appraiser qualifications and appraisal standards.

IRS "Qualified Appraiser" Standards

IRS Notice 2006-96 (issued November 13, 2006; Part III – Administrative, Procedural, and Miscellaneous) states, in pertinent part, that:

"The term 'Qualified Appraiser' means an individual who (1) has earned an appraisal designation from a recognized professional appraiser organization or has otherwise met minimum education and experience requirements set forth in regulations prescribed by the Secretary... [A]n 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...at any time during the 3-year period ending on the date of the appraisal."

² *Federal Register* of August 30, 2010, pp 53172 – 53192. The proposed rule has not yet been issued in final form.

IRS “Qualified Appraisal” Standards

“An appraisal will be treated as a ‘Qualified Appraisal’...if the appraisal complies with all the requirements of Section 1.170A-13(c) of the existing regulations...and is conducted by a qualified appraiser in accordance with generally accepted appraisal standards... An appraisal will be treated as having been conducted in accordance with generally accepted appraisal standards...if, for example, the appraisal is consistent with the substance and principles of the Uniform Standards of Professional Appraisal Practice (USPAP), as developed by the Appraisal Standards Board of the Appraisal Foundation.”

Unlike the general and somewhat vague nature of EBSA’s current appraisal requirements, IRS has established concrete and specific requirements which are designed to eliminate the performance of tax-related appraisals by individuals who objectively lack the qualifications necessary to perform them (for real estate appraisals, a state appraiser certification or license; and, for business valuation and personal property appraisals, a certification from a “recognized professional appraisal organization”); and to require that valuations be conducted in adherence to generally accepted appraisal standards (i.e., USPAP).

As stated above, EBSA has proposed some important changes to its appraisal requirements for prohibited transaction exemptions which move them somewhat closer to the appraisal reform policies at other federal agencies.³ A limited number of additional changes in those requirements – and their extension to all ESOP valuations – would make the requirements fully consistent with those at the IRS (governing the valuation of billions of dollars in noncash charitable contributions annually and for other tax-related purposes); at the banking agencies (in connection with the valuation of property collateralizing extensions of credit); at HUD (regarding insured mortgage loans); and, at many other federal agencies; and, would produce the enhanced beneficiary protections for ESOP valuations that the “fiduciary” approach of the proposed rule contemplates.

DISCUSSION

I. The Proposed Rule’s Unprecedented And Unproven Approach To Ensuring the Integrity of ESOP-Related Valuations Would Be Burdensome and Costly to Appraisers and ESOP Plans; and Ignores the Established, Tested Precedent of the Appraisal Reform Policies of Other Federal Agencies

Adoption of the rule, as proposed, would impose costly and unnecessary burdens on appraisers and on private sector businesses with employee pension and retirement plans. Moreover, the proposed rule seeks to establish valuation requirements – conflict-of-interest free appraisals by highly competent and fully accountable practitioners – which are already in full force and effort for all individuals with professional appraisal designations. As a consequence (and in addition to

³ For example, its proposed definition of a “Qualified Independent Appraiser” would require, in the case of an appraisal of real property, that the appraiser is a member of a professional organization of appraisers that can sanction its members for acts of malfeasance”; and, in the case of a non-real property valuation, require that the appraiser describe his or her “prior experience in valuing assets of the same type.”

the many other deficiencies we find in the proposed rule), it would establish requirements that are redundant to already-existing requirements that are proven and far more cost-effective.

All individuals with professional appraisal designation have already demonstrated their competency in valuing specific types of property by passing an exam and by meeting well-established and widely-recognized experience, training and education (including continuing education) requirements. Additionally, all professional appraisers are accountable for the quality and independence of their work to the state appraiser licensing authority or the recognized professional appraisal organization which awarded the designation.

In short, the net effect of the proposed rule is that it seeks to establish requirements that are already in place and that are currently recognized by all federal agencies and government sponsored enterprises which administer programs or regulate private sector activities, involving appraisals. None of these agencies has recognized a need to impose fiduciary status on appraisers in order to accomplish their appraisal reform objectives. Instead, when these agencies sought to further ensure the integrity of the appraisal processes they administer or regulate, they have adopted the protocols of professional appraisal practice – including reliance on professionally credentialed appraisers and adherence to generally accepted appraisal standards that are consistent with the principles and purposes of the Uniform Standards of Professional Appraisal Practice (USPAP)⁴.

These agencies adopted this approach because they recognized that it is the one most likely to provide the public and taxpayers with a high degree of protection against faulty or abusive valuations. In the case of real property appraisal practice, appraiser licensing agencies in the 50 states and territories oversee their appraiser licensees and often sanction them for violations of USPAP or for other lapses. In the case of business valuation practitioners and personal property appraisers, recognized professional appraisal organizations which teach, test and award credentials to qualified individuals, also sanction their members for violations of USPAP and for other infractions.

⁴ The Uniform Standards of Professional Appraisal Practice (USPAP) are promulgated by the Appraisal Standards Board of the not-for-profit Appraisal Foundation. Congress long-ago recognized the Foundation as the legitimate source of generally-recognized standards and qualifications for the appraisal profession. The purpose of USPAP is to promote and maintain a high level of public trust in appraisal practice by establishing standards of care and ethical conduct by professional appraisers and the manner in which the appraisal must be reported. Two key components of USPAP involve the Competency Rule and the Ethics Rule. The Competency Rule mandates, in part, that an appraiser must be able to identify the problem to be addressed and must have the knowledge and experience to complete the assignment competently. The Ethics Rule states, in pertinent part, that an appraiser “must perform assignments with impartiality, objectivity and independence and without accommodation of personal interests.... An appraiser must not perform an assignment with bias; [and] must not advocate the cause or interest of any party or issue.” If an appraiser knows or learns during the course of an assignment that he or she has any “current or prospective interest in the subject property or parties involved” that information “must be disclosed to the client and in the subsequent report certification.”

II. The Commentary Accompanying The Proposed Rule Fails To Document or Describe The Precise Nature and Extent of the Valuation Abuses Used To Justify The “Fiduciary” Proposal

While our organizations do not doubt that faulty or even abusive ESOP-related appraisals occur from time-to-time, the references to and citations regarding problematic appraisals in the proposed rule provide little or no evidence of them or clues as to their nature and extent. While there may be documentary evidence of a pattern of appraisal abuses in the internal files of the Department or at other agencies, the public record is sparse in this regard. We have reviewed representative examples of publicly available materials (some of which are cited in the proposed rulemaking) that could shed light on problematic valuations in connection with the ESOP program,⁵ but have been unable to locate anything that specifically finds abusive appraisals let alone anything which even remotely demonstrates a pattern of appraisal abuse.

For example, GAO has issued a number of reports on pension plan issues, including the possible deleterious effects of plan consultants who have conflicts-of-interest. GAO’s testimony to Congress on this issue⁶ concluded that there may be a statistical association “between inadequate disclosure [of plan consultants with conflicts of interest] and lower investment returns for ongoing plans, suggesting the possible adverse financial effect of such nondisclosure.” Importantly, however, GAO’s study and testimony did not include even a single reference to a conflict-of-interest by an appraiser. Even GAO’s July 20, 2010, testimony to Congress on defined benefit pension plans and the valuation challenges faced when plans invest in hedge and private equity funds, does not conclude that appraisals have been negligent or abusive; only, that certain assets or interests in assets are difficult to value.⁷

We have also looked at a small, but we believe representative, sample of court cases involving allegations of abusive pension plan appraisals.⁸ The case of *Chow v. Couturier et al* is a good example of what we found. As a result of that case, The Employee Ownership Holding Company (TEOHC) and other parties consented to a restitution payment of more than \$12 million to Plan beneficiaries based, in part, on an abusive overvaluation of the stock of TEOHC resulting in an overpayment to the Plan managers. The Labor Department’s complaint in this case charged that the individual providing valuation services to the plan (Matthew Donnelly and his firm Business Appraisal Institute) and who allegedly was responsible for the overvaluation

⁵ E.g., “Staff Report Concerning Examinations of Select Pension Consultants” May 16, 2005, prepared by the SEC’s Office of Compliance Inspections and Examinations; GAO Report 07-703 “Defined Benefit Pensions – Conflicts of Interest Involving High Risk or Terminate Plans Pose Enforcement Challenges” June 2007; GAO Testimony before House Education & Labor Committee, 09-503T “Private Pensions – Conflicts of Interests Can Affect Defined Benefit and Defined Contribution Plans” March 24, 2009; GAO Testimony before House Education & Labor Committee, 10-915T, “Defined Benefit Pension Plans – Plans Face Valuation and Other Challenges When Investing in Hedge Funds and Private Equity”.

⁶ “Private Pensions – Conflicts of Interest Can Affect Defined Benefit and Defined Contribution Plans,” GAO-09-503T, March 24, 2009)

⁷ GAO’s testimony states, for example, that “hedge funds and private equity face uncertainty about the precise valuation of their investment. Hedge funds may, for example, own thinly traded assets whose valuation can be complex and subjective, making valuation difficult.”

⁸ E.g., *Chao v. Clair Couturier*; *David Johanson*; *Johanson Berenson LLP*; *Robert Eddy*; *James Roorda*; *Matthew Donnelly*; *Business Appraisal Institute*, US District Court Eastern District of California Sacramento Division; *Solis v. Mattingly*, Civil Action Number 2-09-cv207.

“was not qualified to provide an opinion or to value stock because he had no expertise in valuing executive employment benefits, lacked a college degree, lacked any relevant certification, and lacked any relevant license.” In short, the “appraiser” in this case, according to the Department itself, had no appropriate qualifications whatsoever to value the closely held stock held by the plan.

Based on our review of these materials and anecdotal information from members of our organizations who provide ESOP-related valuation services on an ongoing basis, we believe that the problematic appraisals that do occur are largely caused by the selection of individuals to value ESOPs and their assets who lack appropriate valuation education, training and experience; and, who do not adhere to USPAP and its Ethics Rule or to any generally-accepted appraisal standards consistent with the substance and principles of USPAP.

We believe that EBSA’s current appraisal guidance for ESOPs, which fail to establish appropriate appraiser qualifications and appraisal standards necessary to ensure that plans and their assets are reliably valued, may well contribute to the hiring, by plan trustees, of unqualified or under-qualified individuals to provide credible appraisals. EBSA adoption of an appraisal reform rule which relies on professionally designated appraisers and adherence to the Uniform Standards of Professional Appraisal Practice or equivalent generally recognized standards would eliminate many of these problems.

III. We Believe DOL Possesses Significant Statutory Authority to Seek Civil Sanctions and Criminal Penalties Against Parties or Consultants To ESOPs Who Violate ERISA or Who Otherwise Engage In Improper Conduct. If EBSA Is In Fact Powerless To Sanction Appraisers Whose Opinions of Value are Improperly Influenced By Conflicts-of-Interest, It Should Ask Congress For Additional Sanction Authority Sufficient To Deter Wrongdoing

A review of EBSA’s Enforcement Manual suggests that EBSA has wide-ranging powers to investigate and sanction appraisers or others who in engage in improper conduct relating to ESOPs, short of declaring them “fiduciaries”.⁹ However, if the Labor Department concludes that it is powerless to sanction misconduct by appraisers or others under existing authority, it should ask Congress to provide it with additional enforcement powers under ERISA, rather than adopting an “appraiser as fiduciary” rule which will create many more problems than it solves.

IV. Typical E&O Appraiser Policies Do Not Provide Fiduciary Coverage For Appraisers. Absent Such Coverage, Very Few Professional Appraisers Will Assume the Personal Liability That Would Come With Performing ESOP-Related Assignments Under The Proposed Rule

Errors & Omissions policies carried by valuation professionals often exclude coverage when an appraiser is acting in a fiduciary capacity in general. Typical E&O policies carried by business appraisers specifically exclude fiduciary coverage for assignments under ERISA. Although appraisers can purchase fiduciary coverage, they typically have to do so through the purchase of

⁹ For example, the Manual lists “Failing to properly value plan assets as their current fair market value” as an example of an ERISA Civil Violation

a separate policy. The premiums for such specialized policy coverage are extremely costly. As a consequence, adoption of the rule as proposed would inevitably result in a significant increase in the cost of performing an ESOP-related appraisal – costs which would have to be passed through to the companies with ESOP plans. The additional risk exposure appraisers would face as fiduciaries will have a chilling effect on the ESOP valuation community. As appraisers cease performing ESOP valuations because of the prohibitive cost of fiduciary E&O coverage or because they have no appetite to assume the additional risk, the supply of experienced appraisers is likely to greatly diminish with a resultant sharp increase in the costs and even the quality of ESOP appraisals.

Although the added burden on appraisers and the significant additional cost of appraisals under the proposed rule may not be regarded by some as a compelling public policy reason to reject the rule, we believe these negative results deserve the most serious consideration as one of a series of reasons to doubt the efficacy and prudence of the proposal – particularly when there are other approaches to appraisal reform which are proven and far more cost-efficient.

V. We Are Concerned That the Proposed Rule May Be In Conflict With The Ethics Provision of The Uniform Standards of Professional Appraisal Practice, Which Requires Appraisers To Be Independent Of All Parties Or Interests Involved In A Transaction Requiring An Appraisal

We are concerned that because, under the proposed rule, appraisers would owe a special duty of care as a Fiduciary to a particular ESOP party in connection with an ESOP-related valuation, the proposal may be in conflict with the Ethics Rule of the Uniform Standards of Professional Appraisal Practice which requires an appraiser to be independent of all parties or interests involved in a transaction. The Ethics Rule states, in pertinent part, that an appraiser “must perform assignments with impartiality, objectivity and independence and without accommodation of personal interests.... An appraiser must not perform an assignment with bias; [and] must not advocate the cause or interest of any party or issue.” In short, USPAP mandates that appraisers be fully independent of all parties and interests in a transaction, as opposed to owing a special duty of care to any one party as the proposed rule seems to require.

Additionally, we foresee the possibility of a second area of possible conflict or confusion under the proposed rule involving the question of which ESOP party is owed the appraiser’s duty of care as a fiduciary when a valuation is required. For example, we are aware of situations in which the value assigned by an appraiser to the shares of a plan beneficiary who wishes to sell them, is disputed by the beneficiaries who remain in the plan. To whom would the appraiser owe his or her fiduciary duty of care in such a situation? To the seller of the plan shares or to those who remain in the plan? These kinds of open questions further illustrate the potential for myriad problems posed by the imposition of a fiduciary duty on appraisers.

VI. The President’s Recent Executive Order Regarding Executive Branch Avoidance of Burdensome Regulations May Apply To the Proposed Rule

In addition to the many reasons we have advanced in opposition to the proposed “appraiser as fiduciary” rule, we believe that President Obama’s January 18, 2011, Executive Order directing

federal agencies to avoid burdensome regulations, augments the reasons why EBSA should not proceed with the rule, as proposed. While the proposal is well intentioned and addresses a legitimate concern, we believe it does so in a way which the President's Executive Order is designed to discourage. The Order directs agencies to use "...the least burdensome tools for achieving regulatory ends" and to "select, in choosing among alternative regulatory approaches, those approaches that maximize net benefits." Clearly, the least burdensome tool that would accomplish EBSA's purpose is the adoption of the appraisal reform model already successfully in place throughout the government.

VII. Conclusion

Our organizations strongly believe that including appraisers within the definition of "fiduciary" would be a far less effective and far more costly approach to ensuring the independence and integrity of ESOP than the one we are recommending. We respectfully urge EBSA to adopt the appraisal reform system utilized across the federal government – reliance on professionally credentialed appraisers who adhere to the Ethics, Competency and other requirements of USPAP and who are accountability for the quality of their work to the authority which issued their appraiser license or awarded their professional appraisal designation. We would be pleased to offer our assistance to EBSA to accomplish this change.

If you have any questions or if we can furnish additional information, please contact Peter Barash, Government Relations Consultant, American Society of Appraisers, at (202) 466-2221, peter@barashassociates.com or John Russell, Director of Government Relations for the American Society of Appraisers at (703) 733-2103 or jrussell@appraisers.org.

Sincerely,
American Society of Appraisers
National Association of Independent Fee Appraisers