Ethics and the valuer's fiduciary duty and duty to adequately inform the client

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Introduction

Registered valuers are governed by the Valuation Act 1948. The valuers' profession, represented by the Property Institute of New Zealand ("PINZ"), incorporating the New Zealand Institute of Valuers ("NZIV"), and other bodies, has existed for over a hundred years. One of the Institute's objectives is to encourage ethical conduct. The statutory Valuers Registration Board ("VRB") also has jurisdiction over improper, unethical or incompetent conduct, as defined in the NZIV Code of Ethics and "best practice".

Changes in valuation practice in recent years has raised a number of ethical questions. They include the relationship between valuer and client, the duty to adequately inform the client, and compliance with practice standards. In the course of this presentation I hope to address some of these, using hypothetical examples.

The valuers' profession

The 1979 British Royal Commission on legal services thought that there were five main features of a profession:

> (1) A governing body (or bodies) [that] represents a profession and has powers of control and discipline over its members;
> (2) [Mastery of] a specialised field of knowledge. This requires not only the period of education and training...but also practical experience and continuing study of developments in theory and practice;
> (3) Admission...is dependent upon a period of theoretical and practical training in the course of which it is necessary to pass examinations and tests of competence;
> (4) [A] measure of self regulation so that it may require its members to observe higher standards than could be successfully imposed from without;
> (5) A professional person's first and particular responsibility is to their client. The client's case should receive from the adviser the same level of care and attention as the client would himself exert if he had the knowledge and the means.[2]

Sociological studies of professions have traditionally focused on listing those activities which are accepted as professions in an attempt to differentiate profession from non-profession. An alternative approach holds that the ability to obtain and retain professional status is closely related to concrete occupational strategies and to wider social forces and arrangements of power. Such an approach leads to a consideration of the social meaning of occupational tasks (perhaps as easier task with the lawyer or doctor than the architect), the resources behind the

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[2] (1979) vol 1 at para 28, 30.

emergence and the continuation of professionalism, and the social consequences of professionalism.[3]

Sociologists sought to demonstrate that governing bodies were unrepresentative and ineffective regulators; professions lacked the expertise they claimed; admission criteria had little relevance to the actual work of the professions; ethical rules were motivated by economic self-interest and failed to ensure competence; and professionals repeatedly betrayed clients.[4] Producers of a service who succeed in constructing a marketable commodity only become an occupation. To become a profession they must seek social exclusivity. The consumer must acknowledge the value of the producers' services, and must be convinced that they cannot produce the services themselves.[5]

Structural functionalists argue that this is not a conscious, self-interested strategy, but is simply the means by which society ensures that consumers receive quality services. Quality is maintained through controls on entry.[6] To promote competition the free-market advocates would reduce the controls on entry into professions, ignoring the fact that this is a means of maintaining standards in the public interest. If it were indeed true that professional status is for the benefit of the professional, then one would require strong evidence of some countervailing public benefit to justify any monopoly.[7]

The valuers' profession, as a profession, must adhere to high ethical and quality standards. In part this is based on its nature as a profession, and the legal and ethical requirements which this imposes.

The role of ethics

A profession will tend to be concerned with personal confidence of the client in the technical competence of practitioners, and the confidence of the public at large in the integrity and ethical conduct of the profession as a whole.[8]

Because standards cover conduct and competence, both technically and ethically, control must be exercised over both entry into the profession and conduct within it. It follows that by membership practitioners may be subject to sanctions for acts or omissions which do not violate the criminal or civil law.[9] Only statutory regulation can ensure that the disciplinary sanctions are effective.

Controls over the conduct of members of the valuers' profession include personal remedies in tort, contract or equity; the criminal law; an educational standard for entry; procedural and

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[3] Klegon, "The Sociology of the Professions: an emerging perspective" (1978) 5 Sociology of Work and Occupation 259.
[4] Abel, *The Legal Profession in England and Wales* (1988) 7.
[5] Ibid, 10.
[6] Ibid, 12.
[7] McKay, "Professions at risk" [1993] NZLJ 104.
[8] *Royal Commission of Inquiry into Civil Rights* (1968-71) (McRuer Report) Ontario No 1 Vol 3 at para 1161.
[9] Flaus, "Discipline within the New Zealand Legal Profession" (1973) 6 VUWLR 337 at 338.

substantive requirements for admission. Some of these controls belong to the wider law, but some are specific and reflect the fact that members of the profession voluntarily submit to higher standards of conduct than those required by ordinary citizens, and thereby render themselves liable for professional misconduct in addition to any penalty which the common or statute law may impose.[10]

Fiduciary duty

Registered valuers are accountable to the VRB, PINZ and NZIV. Valuers, because of their professional role, owe a fiduciary duty to their clients. While the precise implications of this may be unclear, the general law imposes certain obligations, and the codes of ethics and practice standards of the profession provide others.

Duty to inform clients

Perhaps central to the duty of valuers is the duty of inform clients. Related to this is the question of who precisely is the client, and what are the obligations with respect to the content of the valuation report. I will use a series of examples to illustrate some of the points of tension, and then attempt to draw these together.

Illustration 1.

A valuation company employed a senior valuer who was understood to have a good reputation. The valuation company director became aware that some work completed by the valuer was apparently not up to standard. The valuer was immediately dismissed and went without dispute.

The valuation company then advised their professional indemnity insurer that there would be potential claims. The valuation company, which has a good reputation and longstanding clients, wished to mitigate any damage or loss to the clients by immediately withdrawing the relevant valuation reports to prevent reliance on the reports (proposing a full refund). It is possible that reliance on the documentation had not yet occurred and the valuation company wished to immediately advise the clients to prevent loss to the client and third party who would reasonably be expected to rely on the report, such as a specified financier.

The insurance company's lawyers advised the valuation company not to advise or contact the clients under any circumstances. This prevented mitigation of any loss or damage arising from the reports or reliance on them. The situation was clearly explained by the valuation company to the insurer and their solicitors. There was grave concern at the valuation company, despite the full appreciation of preserving the reputation of the company by not disclosing any defects. It was perceived that the ethical and appropriate thing to do would be to advise the client immediately to prevent any loss. Does the solicitor acting for the insurance company have a conflict of interest in advising the above valuer?

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[10] Abeysuriya, "The Legal Profession" in "Selected extracts from papers given at the [LAWASIA 1993 Colombo] conference" [1993] NZLJ 414.

Response:

A negligent valuer such as this (and vicariously the valuation company) is exposed to legal liability, including negligence. Foreseeable reliance by people in close legal proximity, including banks, creates potential liability for negligent misstatement. Whether or not an action or inaction is negligent is determined by the courts (though, since s 10 of the Valuers Act 1948 requires the profession itself to promote ethical standards, the code of ethics could be influential in guiding a court). The solicitor for the insurance company has a conflict of interest, in that they are the insurance company's advisers, and cannot be seen to be neutral.

Illustration 2.

Where a valuation company provides rating value advice to a Local Authority do they have a conflict of interest if they accept instructions from a rating value objector to undertake a valuation report for the purposes of a rating value objection?

Response:

The PINZ Rules of Conduct, rule 5.0, states that a valuer "shall not accept instructions where there may be, or may reasonably be considered to be a conflict of interest". Receiving instructions in such a situation would create a conflict of interest because they would be potentially utilising information gathered for one client for the advantage of another.

Illustration 3.

A valuation company is approached by a longstanding client to undertake a market valuation of a commercial property for mortgage purposes. The client agrees to pay the fee. Instructions are initially given by that 'client'. A bank then sends 'instructions' (purported instructions) for the valuer to provide the market value report directly to the bank and not provide the report to the paying client who initially instructed the valuer.

Please address ethical issues including the valuer's fiduciary duty to adequately inform the client. Please clarify the legal relationships between (a) the valuer – valuation company, (b) the bank (or other financier/lender) and (c) the initial instructing party who pays the fee.

Note: Some in the finance sector may have a legitimate concern that a member of the public might approach a number of valuers and adopt the highest valuation to present to the bank. It is possible that the bank's concern is simply to protect both the bank and the client by ensuring they obtain a copy of the report before it can be vetoed by the client in favour of a slightly higher value assessment from a different valuer. Information detailed in the valuation report may indeed (other than the value itself) deter the client from purchasing the property at all (regardless of value). It appears that the 'requirements' of the bank are inappropriate with regard to the client-valuer relationship. Perhaps an alternative could be a mutual agreement at the outset that the valuer would release the reports to the bank and client simultaneously, subject to the client's initial approval.

Response:

It is not ethical for the valuer to fail to send the report to the client. This is interference in the contractual arrangement between client and valuer, unless it could be argued that there is an implied or express condition of the contract that the report is to go to the bank only – which is unlikely. The client is not the bank, and the latter has no right to issue instructions to the valuers. Equally, the valuers ought not follow such instructions unless it is clear that this is what the client wishes.

Illustration 4.

There appears to be significant confusion in the valuation profession about who the client is. Members of the public phone, email or otherwise contact the valuation offices with a view to obtaining valuation and property consulting advice. These people pay the fee. The reports are then extended to various organisations usually in the form of a letter and / or valuation report with the letter headed to the organisation to which the report, advice and liability are extended with an additional statement (usually below 'Re') stating the client name.

An example of this can be a valuation report addressed to North Shore City Council Re: Property located at Blue Street, client Mr X. Another example is a market value report for mortgage security purposes regarding a property at 57 Mt Pleasant Street extended to 'Safe Lenders Bank' with client name Mr Y. A further example might be an insurance certificate addressed to insurance company 'RU Cover' regarding a property situated at Calvary Hill with a client name Mr & Mrs Z.

Please define who the client is. Please define the relationship with a third party, who the valuer knows will, or will foreseeable, rely on the advice contained within the report. Who is the instructing party and how can this easily be defined (the entity that makes contact and pays the fee)?

Response:

The client is the client who engages the valuer. Any third party who might foreseeably rely on the valuation report is covered by the law of negligent misstatement. A letter of engagement could easily clarify that the person who initially instructs the valuer – and pays them – is the client.

Illustration 5.

Multi-disciplinary practices exist in the professional world. There are many known examples of these, particularly with accounting and law firms. Recently and for that matter traditionally, there have been valuation companies that provide both 'independent' valuation advice but also are involved in the sale of real estate.

Please address the ethical and legal requirements in New Zealand to prevent conflict of interest in such situations? What would happen if a property were listed for sale (real estate agency) with the same company who were asked to value the property for a prospective purchaser? Can that company be the vendor's estate agent and 'independent' valuer? What if the companies are subsidiaries that all share information?

Response:

The sale of real estate and the provision of valuation reports are two distinct functions which can easily be in conflict. It might in some situations be theoretically possible to adopt "Chinese walls", where there is a clear and complete separation between the operational units responsible for the two functions. In practice, however, it would probably be necessary to disclose the actual or potential conflict of interest, and possibly withdraw from one or other activity.

Illustration 6.

A valuer provides a standard 'market value' report for mortgage security purposes to Mr Joe Bloggs who instructs the valuer and pays the fee. Further to his instructions, the valuer extends the report to a bank. A year later, the bank forecloses on the property and proceeds with a mortgagee sale. The bank contacts the valuer and requests an updated valuation for the purposes of market value assessment and estimated sale price at mortgagee sale.

Can the valuer accept the bank's instructions? Is there a conflict of interest? Does the duty remain strictly with Mr Bloggs or has it been extended to include the bank? What would happen if Mr Bloggs (whom is the only party originally paying the fee) wanted the valuer to update the property valuation but not provide any information or disclose the valuation update work to the bank?

Response:

In this case, the private person who engaged the valuer was clearly the client, and the bank a third party. Bloggs may legitimately ask for an updated report which is not to go to the bank; however, if the bank itself asks for an update, this is actually a new contractual arrangement, and not an "update". To use the information collected for the original client would be a breach of the valuer's duty to that client.

Illustration 7.

The valuer provides a market value for mortgage security purposes to a married couple and accepts the instructions on the basis that the client is 'Mr & Mrs Brown' and the payment is received from Mr & Mrs Brown. Two years later Mrs Brown contacts the valuation company to provide an update valuation for matrimonial/relationship settlement purposes. Can the valuation company act for Mrs Brown? Under what circumstances? Mrs Brown's solicitor contacts the valuer and requests an update valuation to be used in evidence against Mr Brown. The report will relate to the same property as valued for Mr Brown previously.

Note, the value may have changed over that time, but specific details of the property may be important to ascertaining the current value. Such details may be known to the valuer due to his previous work provided for Mr Brown.

Response:

In this case the original client is Mr and Mrs Brown jointly. As partners in the legal sense they have joint and several liability, and are jointly and severally parties to the original contract. Mrs Brown is a new client, and the pre-existing duty to the original clients remains, creating a conflict of interest.

Illustration 8.

Practice Standards require certain things in a valuation report. However, there is an exception rule which provides that a valuer may not fulfill all the aspects of the report, as set out by the Practice Standards and Guidance Notes, where the valuer discloses that the report does not fulfill those requirements and an explanation is given as to why.

The reasons for this can be that the bank approaches a valuer to value a property for mortgagee sale, but no access is available to the valuer and the bank's instructions are to assess the value of the property with or without access. The valuer then proceeds with a 'street side valuation' to give the best information to the bank based on the limited access available to that valuer.

There are circumstances where clients may already know a significant amount of the information that would otherwise be contained in the valuation report. An example of this could be a long-term commercial client with a commercial property who simply requires a review of the rent or market value for consideration in the lead-up to a rent review or proposed sale. The client is familiar with the property details and does not need a full report. There is no third party relying on the report who is unfamiliar with the property.

These exceptions represent many other situations which can generally be divided into two categories: (a): where full information or access is not available to the valuer OR (b): the party to whom the report is provided has the relevant expertise or knowledge of the property and full detail is not necessary.

There can be a third aspect (c): where the property research involved is of a certain value to the client and their additional risk assessment and analysis is undertaken by in-house specialists in relation to a greater portfolio. An example of this might be where Australian banks, in Australia, who hold large mortgage portfolios, are prepared to have a lesser standard of reporting as the overall risk is perceived to be offset by reduced costs for valuation fees. This is due to the diversification of risk across many mortgage interests rather than an individual sale/purchase.

Unqualified and otherwise uninformed consumers within the market rely on professional valuation advice. The advice is usually provided by valuation companies who employ Registered Valuers and rely on the expertise and Practice Standards maintained by such

Registered Valuers working within the New Zealand Institute of Valuers and Property Institute of New Zealand requirements.

The valuer has a fiduciary duty to his or her client. The client is more reliant on the ethics and standards of research, inspection and reporting where the client is otherwise uninformed and does not have expertise in the property field.

Is it unethical for a valuation company to provide desktop or internet based ‘valuations’ that do not fulfill the requirements of a Registered Valuer’s report under the Valuers Act 1948, New Zealand Institute of Valuers and Property Institute of New Zealand Practice Standards and Guidance Notes etc where that valuation company knowingly provides such advice to unqualified and uninformed parties? Such consumers include first homebuyers, retirees or those many members of the public who do not have experience nor expertise in the complexities of the property market.

In many cases, customers are relying on short-form or desktop valuations as if they are of an equivalent standard to a full independent report whereby the property has been inspected and measured and sales evidence more thoroughly analysed with regard to local and site specific factors. Do those who provide short-form and desktop valuations have a duty to fully and comprehensively disclose the significant limitations in reports or value statements provided to members of the public?

Even where these reports are free or of minimal cost and obtainable over the internet but provided by New Zealand companies, the cheapness may be of little compensation to a client who has relied on such advice from a company with a strong marketing campaign where the client later discovers that they have been ill-informed to the tune of hundreds of thousands of dollars. If so, is it fit for the purpose for which it is requested (consumer rights issues)? Even when the report is provided free, does the reporting valuation company extend liability to clients? If not, should this made clear and what would be the point of such free advice?

Where a bank provides its customers with five free such reports as part of a mortgage agreement or marketing campaign does the bank become liable for the inappropriateness (where the bank advises the client to use the valuation company and substandard report and states that this is to make sure that the client pays the “right price”) and inaccuracy of such reports?

Response:

In New Zealand, the client is normally a layperson. Partial reports, which do not meet the requirements of the Practice Standards and Guidance Notes, present a particular risk for them. Whether it is unethical for a valuer to provide a valuation of this sort will depend on several factors, perhaps the most important of which is the extent of the disclosure to the client. The valuer who does not fully inform the client of the limitations of the valuation report could be liable for negligent misstatement, or for a breach of the Consumer Guarantees Act. A bank would not be liable for the accuracy etc of a report which they paid for on behalf of a client. It is inappropriate for a bank to advise a vulnerable client to use a substandard report, rendering them potentially liable in negligence.

Illustration 9.

Considering The Valuers Act 1948 S9 (1) are Rules 149 and 150 of the NZIV Rules ultra vires? Could they be used, or are they of no effect?

Response:

Section 9 of the Valuers Act establishes the NZIV. The Rules of the NZIV are passed by members and approved by the Minister under the Act, and have statutory authority. However, Rules 149 and 150 concern the possibility of the winding up of the NZIV. Since one of the purposes of the Act (as stated in the long title), is the establishment of the New Zealand Institute of Valuers, it might be assumed that the NZIV remains in existence unless and until abolished by further statutory reform. The NZIV is not an incorporated society, and the provisions of Rules 149 and 150 indeed would appear to be ultra vires. The Rules of the Institute (s 16) are meant to cover matters concerned with carrying out the objects of the Institute, and this appears to not include winding it up.

Illustration 10.

Rating Valuations are provided for statutory purposes in accordance with legislation, regulations and the rating rules issued by the Valuer General. Rating Valuations are not provided for mortgage security purposes. Do Local Authorities (or their subcontractors who undertake valuation assessments) bear any liability where banks or the public rely on such Rating Valuations? Do banks who arrange a mortgage security based on Rating Valuation have a duty to their clients (the mortgagor) to clarify whether Rating Valuations are an appropriate method of assessing market value for mortgage security purposes? If subcontractors who provide Rating Value assessments to Local Authorities guarantee or extend these values to mortgagees (or the mortgagors for that matter) do they undertake a liability for the reliability of such information for such a purpose? Do they breach their obligations to the Local Authority in doing so?

Response:

The use of valuation reports for purposes other than that for which they were created could be unethical, and expose parties to liability for negligent misstatement, or for negligence. Local authorities who produce valuation reports may be liable in tort to any other parties where there is foreseeable reliance upon them. This could include banks, though it could be countered that banks ought to know that reliance on rating valuations is not a sufficient safeguard. Banks relying on such valuations could potentially be themselves liable to their clients, if such reliance is held by a court to be in breach of a duty of care.

Illustration 11.

Practice standards require that a mortgage recommendation is provided for mortgage security reports (where valuers provide valuation reports extended to a bank which is advice relied on related to the process of lending funds and taking security over property). Some financiers are “instructing” valuers not to provide mortgage recommendations.

Traditionally, the valuers would provide a mortgage recommendation of no more than 50% for vacant sites and two thirds of the market value (excluding fixed chattels) for improved properties. With adjustments, as appropriate, for each specific property (eg: high land value in relation to very low improvement value).

This percentage amount has been to allow a margin for potential reduction in market value over time (this relates to the cyclical nature of the market and potential for reduced values after a “boom” or “peak of the market”). This also allows for the fact that mortgagors are often well in arrears before the debt assessment and recoveries divisions of the mortgagee will take action to foreclose. This also allows a margin for the costs of sale and the “mortgagee sale” effect on the pricing whereby advertising is usually of a very basic nature and prospective purchasers expect to “pick up a bargain” which often leads to a price below that achievable if the vendor had a “take it or leave it” option.

The mortgage recommendation is often disregarded by the public, financiers and media who, when the market turns, tend to focus on a mythical “over valuation” or “inflated values” as they misunderstand the market value concept as related to the market at a particular date and they lend, or borrow based on temporary values rather than the mortgage recommendations of qualified professionals. Mortgage recommendations also protect the valuers’ clients, the mortgagors, who offer the property for mortgage security to the mortgagee. These maximum mortgage recommendations have been disregarded by the banks for some years now with lending up to 100%.

Where the valuer makes a mortgage recommendation and the valuer has provided the appropriate advice to the financier and the client, this would comply with Practice Standards and Guidance Notes. Where the valuer fails to provide a mortgage recommendation at the request of the bank, the valuer would be required to state why they have not provided a mortgage recommendation and that the report was not in compliance with PINZ Practice Standards. This is becoming a significant issue. The valuer does not assume to be aware of the character, capacity or other collateral of the mortgagor but the recommendation relates to the market factors and foreseeable long-term nature and trends affecting a specific property.

Is it unethical for a Registered Valuer to ignore the Practice Standard requirements at the request of the mortgagee without adequately explaining these issues to the valuer’s client, the mortgagor?

Response:

The valuer should only omit the mortgage recommendation, subject to the client’s prior consent, rather than acting on the instructions directly from the bank. This is because the norm would be to include the mortgage recommendation.

Banks instructing valuers to not provide mortgage recommendations are interfering with the duty of the valuer to the client. Subject to the client’s prior consent, the valuer, in such a case, should indicate in the report that they have not provided a mortgage recommendation at the request of a third party (the bank), and that the report was not in compliance with the PINZ Practice Standards. While the bank knows the risks involved in this practice, the client may not. It would be unethical, and in breach of their duty to the client, to fail to adequately inform them.

Illustration 12.

In Australia, banks pay valuers. Valuers vie for the few major clients. In New Zealand the members of the public pay valuers. Valuers compete for a diverse market of clients and arguably retain greater autonomy. If banks in New Zealand paid valuers to value property and the bank's client (a prospective purchaser) did not receive funding from that bank due to the prospective purchaser's income, could the valuer accept instructions from the prospective purchaser to value the property, or would the valuer have a conflict of interest due to the remaining duty to the bank? Does the bank have the right to stop or not consent to the valuer working on that property for another bank (to prevent losing market share)?

Response:

The valuer would receive instructions from the bank, as this would be the client. They could receive instructions from the prospective property purchaser (cf from the bank now), but it is likely that this would not be accepted; the purchaser does not have the standing of the bank. Once the valuer has accepted the bank as his or her client a duty is owed to that client. Working for another client on that property would create a conflict of interest.

Illustration 13.

An unregistered graduate valuer drives all over a region valuing real property. The graduate emails the reports to a NZ Registered Valuer in another city, or perhaps even overseas. The Registered Valuer never inspects the properties, or the sales. Please address the ethics and legality involved with regard to the duty to the client.

Response:

A registered valuer is responsible both ethically and legally (for instance under the Consumer Guarantees Act) to complete the valuation report him or herself. Completion of the research by an unregistered valuer, under supervision, may be acceptable, but not a report wholly made by an unregistered valuer.

Conclusion

There are a number of serious ethical issues facing the valuer's profession. It behoves the professional bodies, and individual valuers to tackle these head on. The major ones are the identity of the "client", and the contractual, tortious and ethical obligations to them. The second – related – issue, is the role of the bank as "instructor". Thirdly, is the vexed question of the use of valuation reports which are not compliant with the valuers' code of ethics and practice standards.

Non-compliant reports aren't inherently unethical in themselves, but failure to sufficiently highlight the degree of non-compliance, and any other limitations in the reports, would be. It would also render the valuer potentially liable in contract or tort, and under consumer legislation. All or almost all of these difficulties can be avoided or minimised by use of full disclosure and clear letters of engagement.

Since there is no such creature as a registered report, all reports by registered valuers ought to comply with the relevant requirements. Failure to do so must be signalled clearly to the client, and anyone who might reasonably be expected to rely on the report.