



A REPORT
TO THE
ARIZONA LEGISLATURE

Performance Audit Division

Performance Audit

Arizona Board of Appraisal

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REPORT NO. 03-06



Debra K. Davenport
Auditor General

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AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

August 7, 2003

Members of the Arizona Legislature

The Honorable Janet Napolitano, Governor

Ms. Deborah G. Pearson, Acting Executive Director
Arizona Board of Appraisal

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Arizona Board of Appraisal. This report is in response to A.R.S. §32-3604(J) and was conducted under the authority vested in the Auditor General by A.R.S. §41-1279.03. I am also transmitting with this report a copy of the Report Highlights for this audit to provide a quick summary for your convenience.

As outlined in its response, the Arizona Board of Appraisal agrees with all of the findings and plans to implement all of the recommendations.

My staff and I will be pleased to discuss or clarify items in the report.

This report will be released to the public on August 8, 2003.

Sincerely,

Debbie Davenport
Auditor General

Enclosure

PROGRAM FACT SHEET

Arizona Board of Appraisal

Services:

The Board was established in 1990 in response to changes in federal banking regulations that required federally regulated financial institutions to use licensed or certified appraisers for real estate-related transactions and allowed all states to establish agencies to regulate them. The Board has the following responsibilities:

- **Licensing appraisers**—Issuing licenses and certifications to applicants who meet the national education and experience standards. As of January 2003, there were 1,757 active appraisers.
- **Resolving complaints**—Receiving and resolving complaints and taking disciplinary action against appraisers who violate the Uniform Standards of Professional Appraisal Practice. In fiscal year 2002, the Board received 222 complaints.
- **Registering property tax agents**—The Board is required to register property tax agents, who advocate for property owners involved in property valuation matters with the county assessor. As of January 2003, there were 292 registered property tax agents.

Personnel:

The Board consists of the following nine Governor-appointed members, who may serve a maximum of two 3-year terms:

- Four members must be appraisers.
- One member must be a property tax agent.
- One member must be employed by a lending institution that purchases or makes use of commercial or residential appraisals.
- Three must be members of the public.

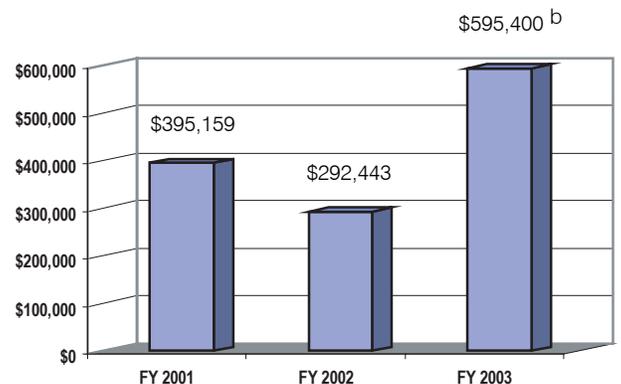
The Board is authorized four full-time equivalent (FTE) positions, which were filled as of May 2003.

Facilities and equipment:

The Board leases space from the Department of Administration in a state-owned building at 1400 West Washington Street in Phoenix. In addition to typical office equipment such as furniture and staff computers, the Board owns ten laptop computers that board members and an Assistant Attorney General use at meetings.

Program revenue:

Fiscal Years 2001, 2002, and 2003 ^a



^a Licensing revenues fluctuate significantly between fiscal years because most of the Board's licensees renew their licenses in odd-numbered years. In addition, licensing fees increased by \$100 for new licenses and by \$200 for renewals as of December 1, 2000. These increases were in effect for only 7 months in fiscal year 2001; consequently, projected licensing revenues are significantly higher for 2003.

^b Fiscal year 2003 revenues are estimates.

Mission:

The Board's mission is to promote quality real estate appraisal in Arizona that protects the health, safety, and welfare of the public.

Board goals:

1. To ensure that license/certification is granted only to candidates who are competent and who meet the Appraisal Qualification Board standards and state standards, and adhere to the current Uniform Standards of Professional Appraisal Practice.
2. To efficiently process applications and license/certify appraisers.
3. To expedite investigation of complaints and provide remedial discipline or take stronger regulatory measures when necessary to protect the public from incompetent and unethical conduct. (This goal is worded to "provide remedial discipline"; however, the Board has statutory authority to take remedial or disciplinary action.)
4. To maintain up-to-date lists of all licensed and certified real estate appraisers, all registered property tax agents, and all approved qualifying and continuing education courses and providers.

Adequacy of goals and performance measures:

Although the Board's goals appear to be reasonably aligned with its mission, auditors identified some problems with the Board's performance measures. For example:

- The Board has efficiency measures for timeliness of applications and complaints. However, it does not currently collect information such as the date an application is received or approved, or the date that a complaint is closed in a database, but rather reports only estimates.
- The Board has an outcome measure under its third goal to report on individuals who recidivate after they have been disciplined, but the Board does not adequately define recidivism. The Board should clarify its definition to include all repeat offenders instead of only those who commit the same violation twice. Further, staff must manually identify these individuals and research individual complaint files to evaluate the Board's performance. The Board should maintain this information in its database.
- The Board reports a rating for customer satisfaction based on a scale from 1 to 8. However, the rating number is based on staff's perception of public and appraiser satisfaction with the Board's performance, rather than on survey results.
- The Board has not appropriately classified all of its performance measures. For instance, the Board's performance measure on disciplinary actions taken during a year is classified as an efficiency measure, but this measure should be classified as an output measure because the numbers of actions are not assessed against other measures, such as timeliness.

SUMMARY

The Office of the Auditor General has conducted a performance audit of the Arizona Board of Appraisal pursuant to Arizona Revised Statutes (A.R.S.) §32-3604(J) and under the authority vested in the Auditor General by A.R.S. §41-1279.03. Unlike most state agencies, the Board does not receive a Sunset review to determine if the agency should be continued, because each state is required by federal statute to have an agency that regulates real estate appraisers. However, the Auditor General's Office reviewed the Board in 1998 in response to a Joint Legislative Audit Committee resolution. After that review, the Legislature established a 10-year review cycle for the Board with the first review due by December 2004.

The Arizona Board of Appraisal was established in 1990 in response to the federal Financial Institutions Reform, Recovery, and Enforcement Act of 1989, which required federally regulated financial institutions to use licensed or certified appraisers for real estate-related transactions, and allowed states to establish agencies to regulate them. Real estate appraisers value, or perform appraisals of, all types of real property, including homes, buildings, and land. The Board's responsibilities include licensing real estate appraisers, resolving complaints regarding appraisers, and disciplining appraisers when violations of standards and statutes are determined. The Board consists of nine Governor-appointed members, including four appraisers, three public members, a property tax agent, and a member who must be employed by a lending institution. The Board derives most of its revenues from licensing and certification fees, and remits 10 percent of its revenues to the General Fund.

Board needs to improve its complaint process and seek statutory authority to recover costs (see pages 9 through 13)

Overall, the Board's complaint-handling process has improved since the the Auditor General's 1998 report (see Report No. 98-6). For example, the Board has begun using contract investigators in place of volunteer investigators and has reduced its backlog of complaints. In addition, the Board is processing most complaints in a

timely manner, and based on a review of the complaint files of four appraisers with multiple complaints, appears to take appropriate disciplinary action for subsequent offenses.

Although the complaint process has improved, it still allows a board member to act both to investigate a complaint and to participate with other board members in adjudicating the complaint. The current process includes an initial file review during which one of the appraiser board members presents the complaint to the Board based on his or her review of the available evidence. The board member then recommends whether the complaint should be dismissed or investigated further. Because of this participation in the investigation, the board member's impartiality in making future adjudicatory decisions is compromised. Further, the Board's initial review process conflicts with the *Attorney General's Arizona Agency Handbook*, which implies that board members involved in adjudicating a complaint should not also participate in investigating the complaint.

To avoid even the appearance of bias, the Board needs to separate the two functions. The Board could modify its current review procedure to require the member who presents the complaint to the Board to refrain from making motions or voting on adjudicatory decisions, such as dismissal, remedial action, or discipline. This option would separate the two functions but would not require additional costs to implement. The Board could also decide to send all complaints first to an in-house or contract investigator for review and investigation. Although this option would eliminate any board members acting in an investigating capacity, it would require additional monies to implement. The Board sent 19 of the 104 complaints it received between July and December 2002 to an investigator. According to the Board, cases might be sent to an investigator if they appear to involve multiple violations.

Regardless of the option chosen, the Board should request statutory authority to recover investigative and hearing expenses arising from complaints that result in disciplinary action. The Board already has this authority for the property tax agents it registers, but not for the appraisers it regulates. This authority should assist the Board in offsetting its complaint-handling costs. At least nine other Arizona regulatory boards have statutory authority to recover investigative and/or hearing costs from licensees who have violated board regulations and statutes. However, to assist the Board of Appraisal in cost recovery as well as other budget decisions, the Board needs to better track its complaint-handling costs. The Board currently lacks a system that can capture costs on a case-by-case basis.

Board needs to provide complete and accurate complaint information (see pages 15 through 18)

Although the Board has implemented a public information policy, additional actions are needed to ensure the public receives complete and accurate information about complaints. Auditors received incomplete complaint information for all five telephone inquiries that they made about appraisers. For example, two of the inquiries regarded appraisers who were on probation, but the callers were not informed that either appraiser was on probation. The Board needs to ensure staff are fully trained on how to provide such information. Another caller was not informed of the nature of the complaint against the appraiser, perhaps because staff currently must determine how to classify complaints on their own. One way to ensure that the public receives this information would be to adopt a system the Board has considered implementing for classifying complaints so that staff can more easily describe the nature of complaints. Finally, the Board is not informing callers about letters of remedial action, which it uses to warn an appraiser to change his or her practice. Although the Board considers these complaints to be dismissed, public record laws require that information about such letters be made available to the public.

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INTRODUCTION & BACKGROUND

The Office of the Auditor General has conducted a performance audit of the Arizona Board of Appraisal pursuant to Arizona Revised Statutes (A.R.S.) §32-3604(J) and under the authority vested in the Auditor General by A.R.S. §41-1279.03. Unlike most state agencies, the Board does not receive a Sunset review to determine if the agency should be continued, because each state is required by federal statute to have an agency that regulates real estate appraisers. However, the Auditor General's Office reviewed the Board in 1998 in response to a Joint Legislative Audit Committee resolution. After that review, the Legislature established a 10-year review cycle for the Board, with the first review due by December 2004.

Board history and purpose

The Arizona Board of Appraisal was established in 1990 in response to changes in federal banking regulations. Specifically, following the savings and loan crisis of the late 1980s, Congress passed the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. The law requires federally regulated financial institutions, such as federally insured banks, to use state certified or licensed appraisers for real estate-related transactions, and allows all states to establish regulatory agencies for the licensing and certification of real estate appraisers.¹ Real estate appraisers value, or perform appraisals of, all types of real property, including homes, buildings, and land. For example, when an individual purchases a home, the mortgage lender will request that an appraiser value the home in order to ensure that the home's value and the mortgage amount are comparable. The Board's mission is to promote quality real estate appraisal in Arizona that protects the health, safety, and welfare of the public.

The federal law also established that appraisers should operate within defined standards of professional practice, which are developed and revised by a nonprofit educational organization called the Appraisal Foundation. These standards, known as the Uniform Standards of Professional Appraisal Practice, guide all real estate appraisers in Arizona and throughout the United States and require, in part, that appraisers act independently to determine the value of real property, use appropriate

Real estate appraisers value homes, buildings, and land.

¹ Federal regulatory agencies include the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration, the Office of Thrift Supervision, the Board of Governors of the Federal Reserve System, and the Office of the Comptroller of the Currency.

methods, and keep for 5 years all materials used in producing an appraisal. In addition, through its Appraiser Qualifications Board, the Appraisal Foundation sets the minimum education and experience requirements for real estate appraisers. Arizona has adopted the uniform standards and the appraiser qualifications in statute (A.R.S. §32-3605(B)).

Finally, the federal law established the Appraisal Subcommittee, which reviews states' regulatory agencies on a 3-year cycle. The subcommittee focuses on how states' agencies operate within federal laws and standards. The Arizona Board's most recent review was completed in October 2002. The review identified some minor issues with the Board's operations, such as the need to submit all disciplinary actions to the Appraisal Subcommittee and the need to correct inaccurate references in its regulations. The Board responded to the Appraisal Subcommittee and developed a plan to address all of the issues identified.

Board responsibilities

The Board's primary functions are licensing real estate appraisers and resolving complaints regarding appraisers. It also disciplines appraisers when violations of standards and statutes are determined. In addition, statute requires the Board to register property tax agents who represent property owners in disputes with county assessors' offices.

- **Licensing**—To ensure quality real estate appraisal in Arizona, the Board issues licenses to qualified appraisers. As of January 31, 2003, there were over 1,700 active appraisers. To become licensed, a candidate must first submit an application to the Board. Under board rules, the Board has 90 days to complete a review of the candidate's application. Auditors determined that the Board reviews applications in an average of 26 days, and actual days for the review ranged from 5 days to 46 days. Once the Board has reviewed the application, the candidate then has up to 1 year to complete a qualifying exam in order to receive a license.

Currently, the Board licenses or certifies three types of appraiser classifications defined by the Appraiser Qualifications Board: licensed real property appraiser, certified residential real property appraiser, and certified general real property appraiser. As shown in Table 1 (see page 3) the appraisers' classifications vary in terms of scope of practice, education, and experience requirements, and each subsequent level of license builds on the previous one, requiring greater education and experience. Licenses and certifications must be renewed every 2 years, and to remain active, an appraiser must complete at least 14 hours of continuing education every year. The Board also provides temporary licenses and certifications for out-of-state appraisers and has reciprocal agreements with

Board fees are currently \$400 for an initial application plus \$100 for the examination fee and \$425 for a renewal. Nonresidential temporary licenses or certificates are \$150.

24 states to license or certify real estate appraisers already licensed in these other states without further education or testing.

Table 1 Number of Licensed and Certified Appraisers with Education and Experience Requirements
As of January 2003

Classification	Scope of Practice	Education ¹	Experience	Number of Active Appraisers
Licensed real property Appraiser	Typical 1 to 4 family residential units valued under \$1 million and complex residential units valued under \$250,000	90 hours	2,000 hours	464
Certified residential real property appraiser	1 to 4 family residential units without regard to value or complexity	120 hours	2,500 hours	661
Certified general real property appraiser	All types of real property	180 hours	3,000 hours	<u>632</u>
Total appraisers				<u>1,757</u>

¹ Includes seven hours of class time on the *Uniform Standards of Professional Appraisal Practice*. Education can be cumulative for higher classification levels.

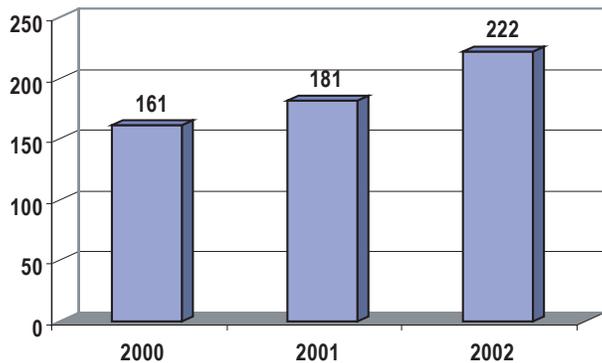
Source: Auditor General staff analysis of the Arizona Board of Appraisal's licensing database as of January 31, 2003, and the appraiser qualification criteria developed by the Appraisal Qualification Board of the Appraisal Foundation as of January 2003.

Many states regulate appraiser trainees, a fourth classification defined by the Appraiser Qualifications Board. The Board does not currently regulate appraiser trainees, but plans to implement regulations for this category in the future. The Board intends to begin the process of changing its rules to include trainees after the Appraisal Qualifications Board publishes new policies on monitoring trainees in the summer of 2003. Additionally, the Board plans to seek statutory authority to assess trainees a nominal fee to cover the administrative costs associated with regulating trainees.

- **Complaints**—The Board is also responsible for handling complaints made against appraisers. Homeowners are the most frequent source of complaints, but many also come from appraisers, such as review appraisers. Review appraisers develop and communicate an opinion or conclusion about the quality of another appraiser's work as part of business, government, or legal situations. When resolving complaints, the Board must determine whether appraisers violated the Uniform Standards of Professional Appraisal Practice. The Board does not have the authority to address complaints regarding fees. Between fiscal years 2000 to 2002, the Board received over 550 complaints (see

Fee disputes are outside the Board's authority.

Figure 1 Number of Complaints Received
Years Ended June 30, 2000, 2001, and 2002



Source: Auditor General staff analysis of Arizona Board of Appraisal complaint database as of February 2003.

Figure 1 for the number of complaints received each fiscal year). In addition, the Board received 104 complaints during the first half of fiscal year 2003.

The Auditor General’s Office has found that Arizona regulatory boards should typically resolve complaints in 180 days or less. Auditors reviewed a random sample of 79 complaints received between July 2000 and December 2002 and found that the Board resolved approximately 53 percent of these complaints in 180 days or less, with 198 days being the average time it took the Board to resolve a complaint. However, the Board has a federal standard that recommends complaints be resolved within 12 months. Of the 79 cases auditors reviewed, all but 7 were resolved within 1 year. Delays in these cases were due to circumstances beyond the Board’s control, such as an appraiser’s family member becoming ill or being unable

to find an investigator.

- **Discipline**—If the Board identifies a violation of Appraisal Standards, it has three disciplinary options available by statute, including censure, suspension, and revocation. Statute also indicates that the Board can otherwise discipline appraisers, and the Board has interpreted the statute to mean that it can define other disciplinary options in its rules.¹ As noted in the text box on this page, the Board has defined probation as a disciplinary option in its rules. As a part of probation, the Board can require that an appraiser complete additional appraisal education classes to keep his or her license, or restrict the appraiser’s practice to certain types of appraising.

The Board has several disciplinary options available

Defined in Statute:

1. Censure
2. Suspension
3. Revocation

Defined in Rule:

Probation

- Education
- Mentorship
- Restriction of practice

Source: A.R.S. §32-3605(B) and A.A.C. R4-46-301.

The Board has also developed a mentorship program as part of its probationary discipline. In some complaints, the Board may determine that the appraiser could improve with additional guidance. In these cases, the Board will require mentorship for the appraiser from someone who has the same type of license and works in the same geographic area. The mentor reviews all of the appraiser’s work and also works with the disciplined appraiser to ensure that the deficiencies identified in the complaint are corrected.

Sometimes appraisers receive additional complaints after being disciplined by the Board. Auditors reviewed the complaint files of four appraisers who received subsequent complaints and found that the Board took appropriate discipline against these four appraisers for their subsequent offenses. For instance, in the initial complaint of one appraiser, the Board and an appraiser agreed to a probationary period with a mentor to settle a complaint. When the appraiser received additional complaints, the Board suspended the appraiser’s license for 60 days and increased the probationary period by 2 years, with at least 6

¹ A.R.S. §32-3605(B).

months of the probationary period to include mentorship. After an additional complaint, the Board suspended the appraiser's license for 2 years or until he could show the Board that he was mentally and physically able to perform appraisals.

The Board took appropriate, progressive disciplinary action against four repeat offenders.

In 2001, the Legislature also provided the Board with a nondisciplinary option. When the Board finds a violation or mistake that does not warrant discipline, such as omitting the property tax costs in the appraisal report, the Board can issue a letter of remedial action instructing the appraiser not to repeat the mistake.

- **Property tax agents**—The Board is also statutorily required to register property tax agents. As of January 31, 2003, there were 292 registered tax agents who act on behalf of property owners involved in property valuation matters with the county assessor. Tax agents must pay an initial \$50 registration fee and a \$25 renewal fee to register with the State to represent property owners. However, they do not have to meet any licensing requirements, such as education, and the Board has limited jurisdiction over their actions.

Staffing and budget

The Board consists of nine volunteers who are appointed by the Governor, including four appraisers. The remaining five board members include a registered property tax agent, who can also be an appraiser; an employee of a lending institution that purchases or makes use of either commercial or residential appraisals and who cannot be an appraiser; and three public members. Board members serve for 3-year terms and may serve for no more than two consecutive terms.

The Board is authorized for four full-time staff positions, which were filled as of May 2003. These positions include an executive director responsible for operations, a regulatory compliance administrator responsible for complaint procedures, an administrative assistant responsible for processing applications and accounts payable, and the administrative secretary, who maintains the front office and telephones and assists other staff when necessary. In addition, the Board contracts with nine investigators to perform investigations of complaints on an as-needed basis.

As illustrated in Table 2 (see page 6), the Board estimates revenues of approximately \$595,400 for fiscal year 2003 and expenditures of \$462,500. The Board mostly derives its revenue from licensing and certification fees. It remits 10 percent of its revenue to the General Fund, and the rest is deposited into the Board of Appraisal Fund. In both fiscal years 2001 and 2002, the Board's expenditures outpaced its revenues

Table 2 Statement of Revenues, Expenditures, and Changes in Fund Balance
Years Ended June 30, 2001, 2002, and 2003
(Unaudited)

	2001	2002	2003¹
Revenues:			
Licenses ²	\$376,144	\$272,801	\$576,203
Charges for goods and services	19,015	15,594	15,891
Other		4,048	
Total revenues	<u>395,159</u>	<u>292,443</u>	<u>592,094</u>
Expenditures: ³			
Personal services and employee-related	197,553	189,410	240,419
Professional and outside services	186,604	167,865	128,017
Travel	10,324	11,041	5,930
Other operating	49,964	72,521	69,551
Equipment	14,387	3,009	11,184
Total expenditures	<u>458,832</u>	<u>443,846</u>	<u>455,101</u>
Excess of revenues over (under) expenditures	<u>(63,673)</u>	<u>(151,403)</u>	<u>136,993</u>
Other financial uses:			
Operating transfers out	7,806	6,803	3,500
Remittances to the State General Fund ⁴	39,753	28,749	60,694
Total other financing uses	<u>47,559</u>	<u>35,552</u>	<u>64,194</u>
Excess of revenues over (under) expenditures and other financing uses	(111,232)	(186,955)	72,799
Fund balance, beginning of year	<u>835,899</u>	<u>724,667</u>	<u>537,712</u>
Fund balance, end of year	<u>\$724,667</u>	<u>\$537,712</u>	<u>\$610,511</u>

1 Fiscal year 2003 amounts recorded after June 30 were not available for this report and are not included.

2 Licensing revenues fluctuate significantly between fiscal years because the majority of the Board's licensees renew their licenses in odd-numbered years. In addition, licensing fees increased \$100 for new licenses and \$200 for renewals as of December 1, 2000. These increases were in effect for only 7 months in FY 2001; consequently, projected licensing revenues are significantly higher for 2003.

3 Includes administrative adjustments from the prior year.

4 As a 90/10 agency, the Board remits 10 percent of its revenues to the State General Fund.

Source: Auditor General staff analysis of the Arizona Financial Information System's (AFIS) *Revenues and Expenditures by Fund, Program, Organization, and Object* and *Trial Balance by Fund* reports for the years ended June 30, 2001 and 2002; and the AFIS *Accounting Event Extract File* for the year ended June 30, 2003.

in part due to reduced fees and in part because most of the Board's licensees renew their licenses in odd-numbered fiscal years. In response to the Auditor General's 1998 audit report (Report No. 98-6, Finding IV), the Board reduced its fees in order to reduce its fund balance, which was nearly four times its annual budget. The Board's fund balance decreased, and in December 2000, the Board raised its fees to its statutory limits.

Audit scope and methodology

This audit focused on the Board's efficiency and effectiveness in licensing appraisers, investigating and resolving complaints, and providing complaint history information to the public. This report includes two findings and recommendations in the following areas:

- The Board needs to further separate its investigation and adjudication processes to avoid the appearance of bias in resolving complaints, and seek statutory authority to recover investigation and hearing costs.
- The Board needs to provide complete and accurate complaint information.

Auditors used a variety of methods to obtain information on the Board and assess its efficiency and effectiveness, including reviewing and following up on findings in the Auditor General's 1998 audit report (Report No. 98-6), reviewing Arizona Revised Statutes, the Board's administrative rules, and appraisal standards, and interviewing board members, staff, and federal reviewers. In addition, the following specific methods were used:

- To determine the timeliness of the licensing and complaint processes, auditors reviewed 31 application files and 79 complaint files that the Board received during fiscal years 2001 to 2003 and calculated the processing times for these files.
- To determine whether the Board is providing an appropriate amount of discipline to repeat offenders, auditors reviewed the complaint files for four appraisers who had received multiple complaints and the Board's actions against these appraisers.
- To determine whether the Board is appropriately separating its investigation and adjudication processes, auditors reviewed the *Attorney General's Arizona Agency Handbook*, attended board meetings, and interviewed board staff, the Board's Assistant Attorney General, and several board members. In addition, auditors contacted seven other Arizona regulatory boards regarding their investigation and adjudication procedures, and received input from the Auditor General's legal counsel.¹
- To determine standards for recovering costs associated with complaint handling, auditors conducted a search of Arizona Revised Statutes and identified nine boards that have statutory authority to recover costs. Auditors contacted

¹ Auditors contacted five Arizona regulatory boards that have the statutory ability to recover all or some of the costs of their disciplinary process: The Arizona Medical Board, Board of Chiropractic Examiners, Board of Cosmetology, Board of Funeral Directors and Embalmers, and Board of Osteopathic Examiners. Auditors contacted two additional boards that do not recover costs: the Board of Dental Examiners and the Naturopathic Physicians Board of Medical Examiners, because they use contract investigators as part of their complaint investigation process.

five of these boards regarding their ability to recover costs. Auditors also collected information on the range of costs the Board incurs for investigation and adjudication by requesting investigation costs from the Board, requesting formal hearing costs from the Office of Administrative Hearings, and interviewing a board investigator and staff.

- To determine whether the Board provides adequate and appropriate information to the public, auditors reviewed the Board's policies and procedures on public information and compared policy requirements to information received from five telephone calls auditors made to the board office requesting information. Auditors also reviewed the Board's complaint and licensing files for completeness, interviewed the Board's Assistant Attorney General, and sought input from the Auditor General's legal counsel.

This audit was conducted in accordance with government auditing standards.

The Auditor General and staff express appreciation to the Board and its staff for their cooperation and assistance throughout the audit.

FINDING 1

Board needs to improve its complaint process and seek statutory authority to recover costs

Although the Board has improved many aspects of its complaint process since its previous audit, the Board needs to make an additional change and could benefit from additional statutory authority in cost recovery. First, the Board needs to separate further its investigation and adjudication functions to ensure that it appears fair and impartial. To resolve this problem, the Board could modify its current process, which would not cost any money, or implement a process similar to other Arizona regulatory boards. The Board should also request statutory authority to recover investigative and formal hearing costs to help address the costs associated with complaint handling.

Complaint process has improved since 1998

Overall, the Board's complaint-handling process has improved since the Auditor General's 1998 audit report (see Report No. 98-6, Finding I and II). At that time, the Board was using volunteer investigators to investigate complaints and had a substantial backlog of open complaints. The Board has discontinued its use of volunteer investigators and now uses contract investigators. The investigators are allowed 30 to 60 days to return an investigation depending on the investigation's complexity, the number of properties involved, and the amount of travel that may be required. Currently, the Board does not report any difficulties in getting timely investigative reports.

The Board has also reduced its backlog of open complaints. In 1998, the Board had a backlog of about 100 complaints, half of which had been open over 300 days. As of February 2003, the Board had only 10 complaints regarding appraisers that have

been open longer than 12 months. In addition, as mentioned in the Introduction and Background (pages 1 through 8), the Board handles most complaints in a timely manner and appears to take appropriate disciplinary action against appraisers with multiple complaints.

Current process does not separate investigation from adjudication

Although the process has improved overall, the Board needs to further separate its investigation and adjudication functions. The current process allows board members who evaluate evidence in a complaint and present this information in board meetings to also vote on the complaint's resolution. This lack of separation compromises the board member's impartiality and is not in line with the Attorney General's guidelines for regulatory boards.

Board members serve as both investigators and adjudicators—The current complaint-handling process cannot ensure that all board members remain objective, because under the current procedure, one member both reviews complaint evidence (investigation) and participates in the Board's decisions on the outcome (adjudication). The Auditor General's 1998 audit found a similar problem, and although the Board has since made changes to the complaint-handling process, the changes have not gone far enough in this regard. The first step in the complaint process is an initial file review during which an appraiser board member conducts an in-depth review of all evidence in the case and identifies the potential violations supported by the evidence. The board member then presents this information to the full Board and recommends whether to dismiss the complaint or refer it for further investigation. Because of this participation in the investigation, the board member's impartiality in making a future adjudicatory decision such as dismissal, remedial action, or discipline is compromised.

The review process conflicts with Attorney General advice—The Board's practice also conflicts with standards established by the Arizona Attorney General's office. Specifically, the *Attorney General's Arizona Agency Handbook* implies that decision-makers such as board members involved in adjudicating a complaint should not participate in investigating a complaint. Because the appraiser board member reviews evidence as an expert and cites violations, he or she becomes part of the investigation and therefore should not be part of the adjudication. The Board's lack of separation between the investigative and adjudicative processes can give the appearance that the Board is not resolving complaints fairly.

The *Arizona Agency Handbook* implies that decision-makers not be involved in complaint investigations.

Board should modify its complaint process

To avoid the appearance of bias, the Board needs to change how its members participate in the complaint process. The least costly option for the Board is to modify its current procedure to require that the member who presents the complaint information to the Board in the initial review not be part of deciding what adjudicatory action to take. This member could participate in presenting complaint information, discussing the complaint with board members, and making a recommendation to dismiss the complaint or send it to investigation. However, the board member would recuse himself or herself from making motions or voting on both current and future adjudicatory decisions on the complaint such as dismissal, remedial action, or discipline. This option would allow the Board to separate its investigation and adjudication functions without incurring additional costs.

The Board could consider another option to separate its investigation and adjudication functions; however, this option would be more costly for the Board and more difficult to implement. At least seven other Arizona regulatory boards have staff or contract investigators who investigate all complaints prior to board review. For instance, the Board of Cosmetology has a staff investigator who investigates complaints before the board reviews them. The Board of Dental Examiners assigns all complaints to a contract investigator before board review. Using an in-house or contract investigator would allow the Board to completely separate its investigation and adjudication functions by eliminating the initial review. However, it would also result in additional costs to hire an in-house investigator or send all complaints to a contract investigator. Currently, most complaints do not go to an investigator. For example, between July and December 2002, the Board sent only 19 out of 104 complaints to an investigator. According to the Board, a complaint might be sent to an investigator if a large number of potential standards violations are identified. However, if the complaint involves minor violations, it would not be sent to an investigator.

Reviewing board member should be recused from future adjudicatory decisions.

Board should seek statutory authority to recover costs

The Board should request statutory authority to recover investigative and hearing expenses arising from complaints that result in disciplinary action. The Board already has this authority for the property tax agents it registers but not for the appraisers it regulates. This authority should assist the Board in offsetting its complaint-handling costs. Some other Arizona regulatory boards already have this authority. However, to assist it in cost recovery, as well as other budget decisions, the Board needs to track its complaint-handling costs on a case-by-case basis.

Statutory authority to recover costs could offset complaint-handling expenses.

Complaint-handling costs can be high—The Board should seek statutory authority to recover some or all of the complaint costs from appraisers found in violation of the appraisal standards. Doing so would assist in offsetting expenses. The Board's complaint workload has increased by 38 percent, from 161 complaints received in fiscal year 2000 to 222 in 2002. To handle complaints, the Board incurs both investigative and formal hearing costs, among other items. Current costs for investigations vary by complaint. For example, the investigator who was used most often in fiscal year 2003 (through April 2003) charged an average cost of about \$1,400 per complaint, with costs per complaint ranging from \$600 to \$2,600.

Additionally, the Board uses the Office of Administrative Hearings (OAH) for some formal hearings. In this capacity, OAH holds hearings before an administrative law judge in which the appraiser's and the Board's representatives present evidence regarding the complaint. After testimony is heard, the judge makes a recommendation on the case to the Board, which the Board may either accept or reject. Over the past several years, the Board has increased its use of OAH. In fiscal year 2001, OAH heard five formal hearings for the Board. That number rose to 13 in fiscal year 2002 and to 18 in the three-quarters of fiscal year 2003. While OAH's annual bills for hearings vary according to the previous year's costs, they can be significant, depending on the time individual complaints consume. For example, the cost for one OAH hearing billed in fiscal year 2003 was about \$1,150. However, the cost for a longer, more complex case, which had several hearings in fiscal years 2001 and 2002, was almost \$10,000.

Some other Arizona boards can recover costs—At least nine Arizona boards have statutory authority to recover investigative and/or hearing costs from licensees who have violated board regulations and statutes.¹ Although there is no clear pattern as to the specific expenses these boards define as investigative or hearing costs, seven boards can collect formal hearing costs from their licensees. Three of the boards, the Board of Chiropractic Examiners, the Board of Cosmetology, and the Board of Funeral Directors and Embalmers, can also require licensees to pay investigative costs. The Board of Funeral Directors and Embalmers also may assess the licensee expenses incurred with conducting an informal interview.

Tracking costs is necessary for cost recovery—To have sufficient information to recover some of its complaint-handling expenses, the Board needs to begin tracking its costs per case. Although the Board has information on the hourly rates of contract investigators and receives invoices from them, it does not keep track of investigative costs on a case-by-case basis. Additionally, the Board does not track formal hearing costs for individual cases. Formal hearing costs would include OAH costs and may also include the costs of an Assistant Attorney General who represents the State on the complaint, investigator testimony costs, and court transcripts costs. In addition, the Board needs to identify board-specific costs, such as costs for subpoenas. Depending on the extent of the statutory authority the Board seeks, it

The Board needs to track complaint-handling costs on a case-by-case basis.

1 Arizona Medical Board, Board of Athletic Training, Board of Chiropractic Examiners, Board of Cosmetology, Board of Optometry, Board of Osteopathic Examiners in Medicine and Surgery, Board of Physical Therapy, Board of Funeral Directors and Embalmers, and Regulatory Board of Physician Assistants.

should determine which complaint costs it specifically needs to track to appropriately assess expenses.

Cost information can also guide the Board in budget decisions—The Board also can use complaint-handling cost information to assist in making decisions on budget issues. For instance, tracking costs would allow the Board to determine better whether it would be feasible to hire a staff investigator under its current budget. Additionally, the Board’s fund balance has decreased since fiscal year 2001, and the Board is considering raising fees to ensure that it maintains a fund balance. If it is allowed to recover costs from complaint handling, it can use cost information to determine how much it will need to raise fees.

Recommendations

1. The Board should revise its complaint-handling process to ensure that it remains fair and impartial by doing one of the following:
 - a. Requiring board members who review and present evidence on complaints to recuse themselves from voting on any adjudicatory decisions.
 - b. Referring all complaints to a contract investigator or in-house staff investigator for investigation before any board review.
2. The Board should request statutory authority to recover investigative costs and the costs of hearings for complaints against appraisers that result in disciplinary action.
3. The Board should define the specific costs associated with complaint handling and track these costs by individual complaint.

FINDING 2

Board needs to provide complete and accurate complaint information

Although the Board has implemented a policy that specifies the information it will make available to the public regarding complaints, improvements are needed to ensure that this policy is followed. Auditors received incomplete information in each of the five telephone inquiries they made about appraisers with complaints. The Board needs to ensure staff are fully trained on how to provide complaint information. The Board should also consider adopting a system for classifying complaints so that staff can more easily provide information about the nature of complaints, as required by its policy. In addition, the Board is currently keeping letters of remedial action confidential, even though public record laws require that these should be made available to the public.

Public not provided with complete complaint information

Although the Board has made improvements regarding public access to information since the Auditor General's 1998 audit report (see Report No. 98-6, Finding III), the public still does not receive complete information on complaints. The previous audit found that board staff did not consistently provide the public with complete and accurate information by telephone. To address this concern, the Board implemented a public information policy, which requires that the public receive information on the disposition and nature of the complaints and contains examples of what information could be given regarding the nature of the complaint. It is important that the public receive information on both complaint disposition and nature. Disposition information explains to the public the sanctions that the Board imposed on the appraiser, such as the appraiser's consent to being on probation. Information on the nature of complaints explains to the public what type of violation the appraiser committed, such as a major breach in ethics.

Auditor General staff made telephone calls to the Board to request complaint histories on five appraisers, but in each case, board staff did not provide the full information required by the Board's public information policy. In some cases, the number and type of complaint actions taken against the appraiser was not explained; in others, important information was not divulged about the nature of the complaint. Specifically:

- **Incomplete complaint histories**—In three instances, board staff did not provide complete and accurate information on the appraisers' complaint histories. Two of the calls regarded appraisers who were on probation, but the callers were not informed that either appraiser was on probation. Rather, in one instance, the caller was told that the appraiser had received one anonymous complaint that was still under investigation, and in the second instance, the caller was told that the Board had not received any complaints regarding that appraiser. The third call regarded an appraiser who had one dismissed complaint. The caller was informed that the appraiser did not have any complaints.
- **Incomplete information on nature of complaint**—In the two remaining calls, the callers received complete and accurate information regarding each appraiser's complaint history; however, the callers received little information on the nature of the complaints. In one instance, the caller was informed that the appraiser received a due diligence letter for violating the appraisal standards' competency section. The caller was also informed that the appraiser received a second due diligence letter, but was not informed of the nature of this complaint. In a second call, the caller was told that the appraiser had received a due diligence letter, but that the complaint was "not serious in nature."

Additional steps needed to ensure complete information provided

Since the Board already has an appropriate public information policy, other measures are needed. Specifically, the Board should take two additional steps to ensure that consumers receive complete and accurate complaint information:

- **Train staff on how to provide information to the public**—The Board has a small staff and does not do any formal training on procedures. Although the Board clarified its public information policy in April 2003 to indicate that only the executive director and the regulatory compliance administrator can provide complaint history information to the public, the Board needs to ensure that all staff understand who can provide complaint information. In addition, as new staff are hired, the Board should ensure that they fully understand the policies and procedures regarding public information and their role in providing that information.

- **Develop means for classifying complaints**—One reason the public may not receive consistent and complete information on the nature of complaints is because the Board currently does not classify the nature of complaints and board staff must determine on their own how to describe the nature of complaints. The Board has considered implementing a set of guidelines that rank from one to five the violations found in a complaint, with one being the least serious type of violation. Each ranking has a description of the types of violations that it would include. For instance, a complaint that is given a rank of level 2 would be one in which a series of mistakes affected the appraisal’s credibility. The Board should implement these guidelines now so that board staff could use them to easily and quickly provide the public with complete and consistent information on the nature of complaints.

The Board should implement a complaint classification system.

Information needed about letters of remedial action

To comply with public records laws, the Board should also inform consumers about complaints resulting in letters of remedial action. The Board received statutory authority to take remedial action in 2001. The Board uses letters of remedial action when it wants to warn an appraiser to change his or her practices in order to avoid future problems. Letters of remedial action usually instruct the appraiser not to repeat the mistake, but they may also require the appraiser to take classes. The Board requires that complaints in which an appraiser receives a letter of remedial action be classified as dismissed and considers a letter of remedial action nondisciplinary. Therefore, anyone seeking information on an appraiser’s complaint history would be told that the appraiser had a dismissed complaint, but not that they had received remedial action.

The Board uses letters of remedial action to resolve complaints it deems not serious in nature.

However, according to public records laws, documentary materials made by any government agency as a result of public business and as evidence of the organization’s decisions are public records.¹ A letter of remedial action is a public record because it results from decisions made in an open meeting and documents the Board’s action involving an appraiser. Thus, the Board should develop a way to ensure that the public is also informed about letters of remedial action when seeking information about appraisers’ complaint histories. One way to do this would be to create two categories of dismissed complaints, one of which includes remedial action.

¹ A.R.S. §§39-121.01(B) and 41-1350.

Recommendations

1. The Board should ensure all staff are fully trained on how to correctly provide complete and accurate complaint information to callers requesting information about appraisers' past performance.
2. The Board should implement a method of classifying complaints that staff can use to provide complete and accurate information about the nature of complaints.
3. The Board should inform the public about letters of remedial action. It could do so by developing two categories of dismissed complaints, one being dismissed but with a letter of remedial action sent to the appraiser.

AGENCY RESPONSE

July 30, 2003

Ms. Debra K. Davenport, CPA
Auditor General
2910 North 44th Street, Suite 410
Phoenix, AZ 85018

Re: Audit of the Arizona State Board of Appraisal

Dear Ms. Davenport:

The Board has received a final draft of your audit of the Arizona State Board of Appraisal dated July 24, 2003. Enclosed is the Board's response to your audit. A diskette is also enclosed with this response.

The Board and its staff would like to express appreciation to your auditing staff for performing the audit with as little disruption of the Board's business as possible.

If you have any questions regarding the enclosure, please do not hesitate to contact me.

Sincerely,

Deborah G. Pearson
Acting Executive Director

Enclosures

RESPONSE TO FINDING 1
BOARD NEEDS TO IMPROVE ITS COMPLAINT PROCESS
AND SEEK STATUTORY AUTHORITY TO RECOVER COSTS

Audit Recommendations

1. The Board should revise its complaint-handling process to ensure that it remains fair and impartial by doing one of the following:
 - a. Requiring board members who review and present evidence on complaints to recuse themselves from voting on any adjudicatory decisions.
 - b. Referring all complaints to a contract investigator or in-house staff investigator for investigation before any board review.

Board's Response: The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented. To resolve any perceived conflict of interest, the Board voted at its July, 2003, meeting to implement by December 31, 2003, a new procedure whereby complaints will not be assigned to an individual Board member for summary at the Board meetings. Instead, staff will summarize the complaints to be followed by open discussion, comments, recommendations, motions and voting by all Board members. As in the past, all Board members will be furnished copies of all complaint files for review prior to the Board meetings.

2. The Board should request statutory authority to recover investigative costs and the costs of hearings for complaints against appraisers that result in disciplinary action.

Board's Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented. The Board will be approaching the legislature in calendar year, 2004, requesting statutory authority to recover investigative and formal hearing costs associated with complaint handling and resolution.

3. The Board should define specific costs associated with complaint handling and track these costs by individual complaint.

Board's Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented. The Board has already implemented a process whereby the costs of investigations, formal hearings before the Office of Administration, and court reporter costs are being tracked by individual complaint.

**RESPONSE TO FINDING 2
BOARD NEEDS TO PROVIDE COMPLETE AND
ACCURATE COMPLAINT INFORMATION**

Audit Recommendations

1. The Board should ensure all staff are fully trained on how to correctly provide complete and accurate complaint information to callers requesting information about appraisers' past performance.

Board's Response: The finding of the Auditor General is agreed to and a different method of dealing with the finding will be implemented. Of the four full-time employees, all are new hires, except one. Because there will be a tremendous learning curve for all new staff members and to ensure that accurate information is furnished, only the established employee will provide callers with information about appraisers' past performance. As each new staff member demonstrates the ability to understand the process, he/she will be trained on how to accurately provide callers with information.

2. The Board should implement a method of classifying complaints that staff can use to provide complete and accurate information about the nature of complaints.

Board's Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented. After a complaint has been adjudicated, the Board will classify the complaint as: (a) dismissed with no violations (nondisciplinary); (b) dismissed with violations and a letter of remedial action (nondisciplinary); or (c) findings of violations of USPAP, statute or rule (disciplinary). The caller will be advised of the classification. If violations are found, information regarding the violations will be made available to the caller either verbally or by requesting that the caller file a Public Records Request Form to obtain a copy of the final finding. If a complaint has not been resolved, a caller will be advised that a pending complaint exists.

3. The Board should inform the public about letters of remedial action. It could do so by developing two categories of dismissed complaints, one being dismissed but with a letter of remedial action sent to the appraiser.

Board's Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented. Although there was some initial confusion, the public is now informed of letters of remedial action.

Performance Audit Division reports issued within the last 12 months

02-01	Arizona Works	02-11	Department of Health Services—Health Start Program
02-02	Arizona State Lottery Commission	02-12	HB2003 Children’s Behavioral Health Services Monies
02-03	Department of Economic Security—Kinship Foster Care and Kinship Care Pilot Program	02-13	Department of Health Services—Office of Long Term Care
02-04	State Parks Board—Heritage Fund	03-L1	Competitive Electric Metering, Meter Reading, and Billing and Collections
02-05	Arizona Health Care Cost Containment System—Member Services Division	03-01	Government Information Technology Agency—State-wide Technology Contracting Issues
02-06	Arizona Health Care Cost Containment System—Rate Setting Processes	03-02	Registrar of Contractors
02-07	Arizona Health Care Cost Containment System—Medical Services Contracting	03-03	Water Infrastructure Finance Authority
02-08	Arizona Health Care Cost Containment System—Quality of Care	03-04	State Board of Funeral Directors and Embalmers
02-09	Arizona Health Care Cost Containment System—Sunset Factors	03-05	Department of Economic Security—Child Protective Services—Foster Care Placement Stability and Foster Parent Communication
02-10	Department of Economic Security—Division of Children, Youth and Families, Child Protective Services		

Future Performance Audit Division reports

Arizona State Board for Charter Schools

Department of Commerce