THE JCK MANAGEMENT STUDY CENTER

WHY YOU NEED APPRAISAL EDUCATION

Appraising is a profession.
Those who practice it must understand that profession's standards, principles and procedures

PROFITS VS. PITFALLS
IN PROFESSIONAL APPRAISING

[Author's note: This article should not be considered a replacement for formal appraisal education. Rather, it is an introduction to some of the basics of appraising, a primer that provides definitions and examples that should be helpful to current practitioners. It is intended to help jewelers assess their proper role in offering appraisal services.]

The appraising profession can provide all the advantages that come with offering professional services. But the benefits and profits often appear overshadowed by ever-growing pitfalls. Rather than scare off a hopeful appraiser, such pitfalls should encourage him or her to gain more knowledge about appraising. This article hopefully will clear up some misconceptions and persuade those who wish to reap the profits to obtain the professional appraisal education they need.

The winds of change: Since the late 1970s, the jewelry industry has experienced an intellectual revolution on the issue of appraising. Many jeweler appraisal practitioners now actively, even aggressively, seek knowledge and standards. An undercurrent of unrest and concern agitates many others. Meanwhile, the number of independent (non-merchant) appraisers has grown markedly over the past decade.

An artist might depict all this activity as a cyclone in which merchant practitioners spin in a cycle of concern and confusion. They hope to find the source of the appraisal problem and a panacea to cure all its woes.

This picture isn't unique to the gem and jewelry trade. It applies equally well to the antiques, fine arts, household contents, machinery and equipment trades, as well as to members of the insurance industry, the legal and business communities and a host of state and federal regulators.

A number of ethical and procedural quandaries have plagued merchants for as long as appraisals have been written. In the late 1980s, for example, inflated donation appraisals drew highly publicized government penalties. Most jewelers never wrote such exotic federal tax appraisals. But court decisions that shot down long-standing beliefs and traditions caused many to wonder about procedural problems with the types of appraisals they did perform.

A barrage of negative appraisal-related problems in the 1980s changed concern and caution to fear. Many jewelry industry leaders tried to fill the void left by a lack of accepted standards in a mad search for panaceas that would answer all appraisal questions and drive away the problems.

Appraisal band-aids: Many well-intentioned solutions were offered; some should sound familiar:

- "We appraise only items that we sold" was one common approach.
- "We appraise any used jewelry, but we will only appraise new jewelry that we sold" was an expanded version of this position.
- "We do appraisals for insurance only" was another approach, sometimes followed with "and an occasional estate or resale appraisal."
- "You should appraise only at your own selling price," proclaimed one jewelry organization.
- "If your appraisal is no more than a restatement of your selling price,

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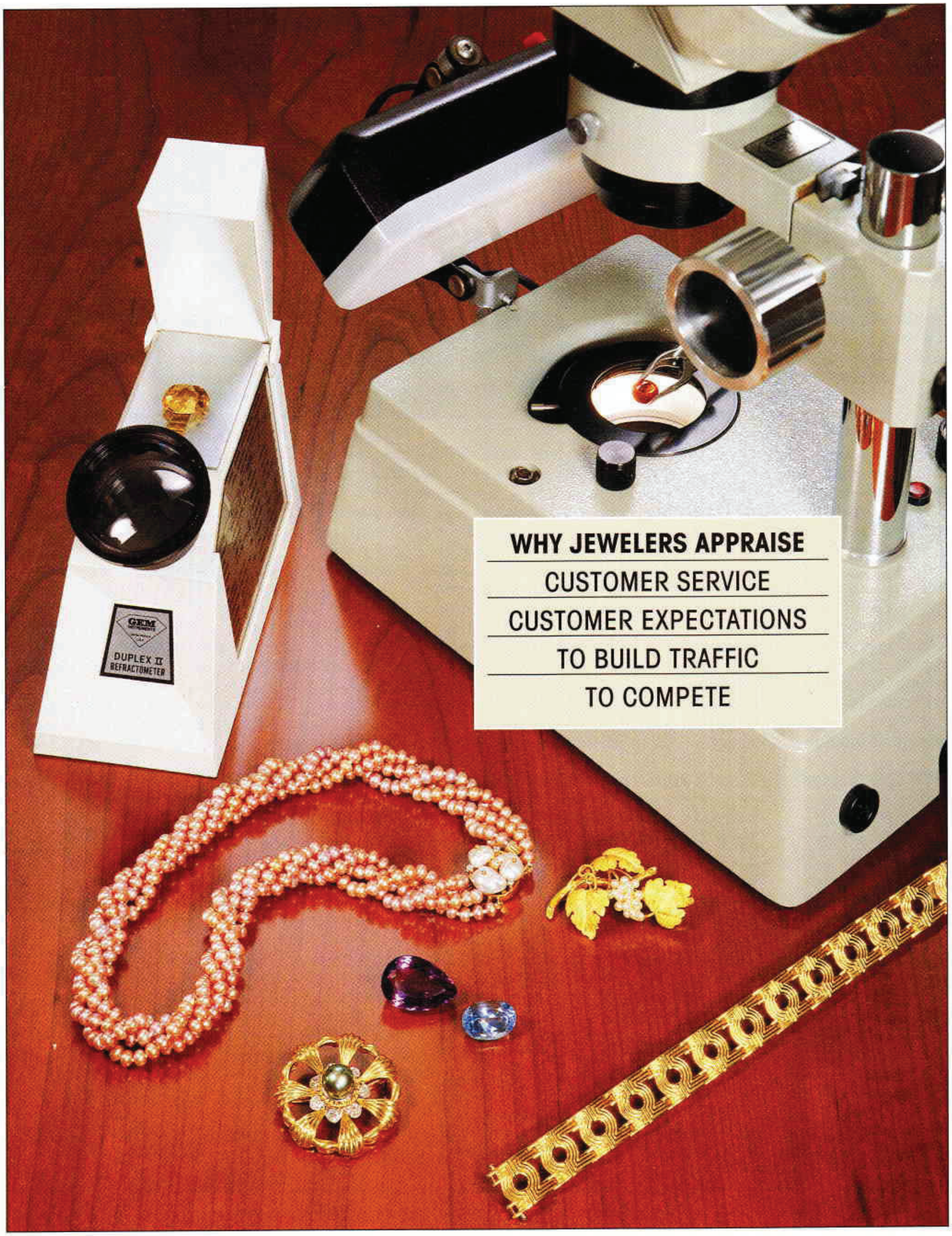
Rosen was one of the principal developers of ISA's Certified Appraiser of Personal Property (CAPP) program and was ISA's primary developer and instructor in the CAPP Core Appraisal Principles Courses, as well as the CAPP Advanced Appraisal Principles and Expert Witness courses. He served as chairman of ISA's Gems & Jewelry Division from 1982 through 1992, education chairman from 1982 through 1993 and vice president for personal property standards and qualifications until resigning from ISA last October. He also developed and was primary instructor for the CAPP "Appraisal of Gemstones" specialty course, and co-developer and instructor of the CAPP specialty course on "The Appraisal of Jewelry: Mid-20th Century to the Present."

Born into a diamond importing family, Rosen has been involved in the jewelry industry since 1976 as a diamond and colored stone wholesaler, retail salesperson and gemological appraiser, independent appraiser and educator. Currently, he is under contract to a major industry organization to write a new series of residence and home-study courses on appraisals. He also serves as a consultant to other appraisers, publishes sample appraisal report language and is developing a new appraisal principles newsletter and international networking electronic bulletin board.

Opposite page: An appraiser's primary role is to provide information on the worth of an item. Such valuation often requires varying amounts of evaluation, as well – including but not limited to identification and grading of materials, plus authenticating the background or origin of a piece. Jewelry supplied by Elaine Cooper & Company Ltd., Philadelphia, Pa. All photos by Robert Weldon, senior editor.


GEM
DUPLEX II
REFRACTOMETER
WHY JEWELERS APPRAISE
CUSTOMER SERVICE
CUSTOMER EXPECTATIONS
TO BUILD TRAFFIC
TO COMPETE

then you should call it 'an estimate of replacement cost in our store,'" said one appraisal education program.

• "You should write insurance appraisals at 25% more than your selling price to cover your customer for future inflation," suggested another jewelry organization.

• "You can't appraise items you've sold because you have a conflict of interest," cried a new breed of independent professional appraisers.

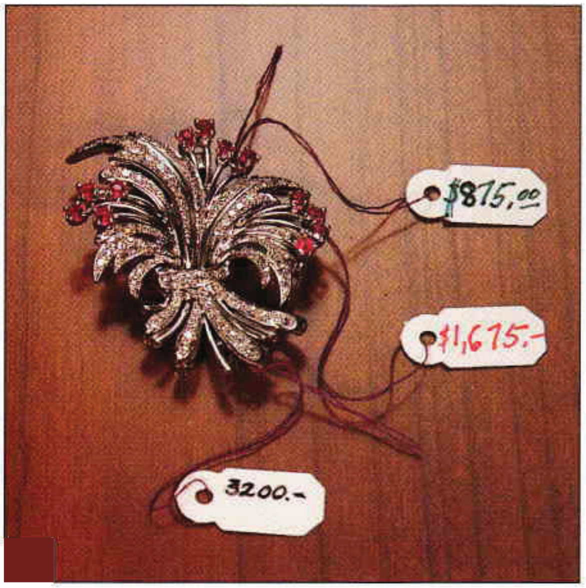
• "You can't write accurate appraisals unless you're buying and selling, putting your money where your mouth is," some jewelers retorted.

• "Retail replacement value ...appraisals must state...that appraisers' opinions as to the value of jewelry vary by as much as 25%" became the law in a major metropolitan area.

• "A qualified appraiser is one who is qualified," proclaimed the U.S. Congress in the 1984 Deficit Reduction Act (which regulates appraisals for charitable contributions of property valued at more than $5,000).

• "When providing appraisals, jewelers are prohibited from charging fees which are based on a percentage of the value," announced the Commonwealth of Pennsylvania in the mid-1980s.

• "You should never appraise a mounted diamond in the setting unless you give a spread of quality grades," claimed a jewelry industry protection organization.



A single item at a certain time can have many different types of values. In addition, the same item often sells at different prices in a capitalist sytem. That's why appraisers are needed.

• "Should the guides [for the jewelry industry] be expanded to include appraisals of jewelry in addition to sales and offers to sell jewelry?" asked the Federal Trade Commission in 1992.

• "We no longer do appraisals. There's no way to do them right and we don't need the problems," concluded many jewelers.

An overabundance of such well-intentioned Band-Aid "solutions" plagued the profession. But black-and-white solutions wouldn't solve variable problems. Only one could really treat the disease: professional appraisal education, testing and certification.

The gathering storm: As appraisal issues began to attract headlines and lawyers in the late 1980s, jeweler-appraisers suddenly faced the threat of legal action for violating "express warranties" established by their point-of-sale appraisals. Ever more likely were negligence and damage suits by clients and consumer advocates or charges of appraisal-related disparagement and unfair trade practice from competitors. The merchant-appraiser community also faced a slew of new government regulations and/or penalties.

At the same time, personal property appraisal associations increased their visibility and offered the first professional appraisal courses. While such education was the panacea, it sadly got mired in battles with traditionalists and among the proliferating and competing appraisal groups.

In the early 1980s, I was guilty of panacea-mongering. I was among the many sincere individuals giving well-

TIMELINE OF SOME IMPORTANT APPRAISAL-RELATED COURT DECISIONS ON SELECTED TOPICS

Guggenheim vs. Rasquin

Subject: Original cost as a measure of fair market value.
Case: "Cost is cogent evidence of value.... Cost in this situation is not market price in the normal sense of the term. But the absence of market price is no barrier to valuation."

– U.S. Supreme Court

1941

Hughes vs. Potomac Insurance Co. of the District of Columbia

Subject: Role of appraisers in making an award for damages when serving on an insurance claims panel.
Case: "The function of appraisers [when serving on an insurance claims panel] is to determine the amount of damage resulting to various items submitted for their consideration. It is certainly not their function to resolve questions of coverage and interpret provisions of the policy."

– California Court of Appeal, First District

1962

Tripp vs. Commissioner

Subject: Appraiser's opinion must be based on facts. (Donation case involving jewelry of antiquity that was bought in Europe).
Case: "...the record discloses that the opinion testimony of these witnesses was almost wholly subjective in character. And, opinion evidence which does not appear to be based upon disclosed facts is of little or no value. Petitioner's witnesses failed to support their conclusions as to value with facts of convincing probative value."

– U.S. Court of Appeals, Seventh Circuit

1964

Goldman vs. Commissioner

Subject: For donations (or estate taxes), the fair market value must be sales to the ultimate consumer.
Case: [paraphrased] "Public" in the fair market value definition means sales to an ultimate consumer. Fair market value cannot be based on sales to a dealer buying for resale.

– U.S. Court of Appeals, Sixth Circuit

1967

intentioned but insufficient answers. Specifically, we suggested that appraisals would be more professional if only they were more gemologically intensive, with longer descriptions. Gemology obviously *is* important to gemological appraising, but many now realize that an understanding of appraising is even more vital.

So why appraise? Considering all the problems, why bother with appraisals? In short, because the needs, benefits and profits outweigh the pitfalls. That's why many jewelers continue to appraise, despite an increase in apparent appraisal hazards.

It helps that the education vacuum is slowly but surely being filled. Although standards for appraising personal property are in the infant stage, good courses and education programs, testing and certification do exist. And more comprehensive advanced courses are being developed.

Here are some specific reasons why jewelers still offer appraisal services:

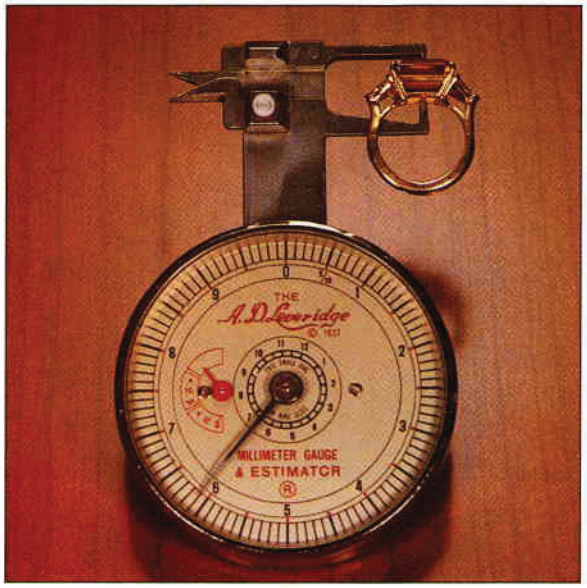
1. Customer service. Appraisal services often are required by customers who appreciate a full-service establishment.

2. Customer expectations. Customers have come to expect insurance appraisals with items they buy.

3. Traffic building. A well-advertised appraisal service can bring new customers into the store.

4. Competition. The jeweler who fails to offer a point-of-sale appraisal or to recommend the services of an independent appraiser fears a customer may go to the competition for one. Jewelers complain that appraisals by competitors often result in a "killed" sale or a stolen customer.

5. Gemological background. Some jewelers offer appraisals under the misconception that their gemological training alone equips them to do so.



Can a diamond or other gem be appraised in the setting? Of course; a Leveridge gauge is one of the tools used. The issue is not whether to do it, but how and when to do it and how to be clear in writing a report just what was done and why.

What about the apparent problems? The main ones are lack of professional appraisal education and methodology.

The first step is to recognize that appraising *is* a profession. Being a competent, safe practitioner requires knowledge of the profession's standards, principles, procedures and methodology. Most apparent problems disappear once the nature of appraisal professionalism and the appraisal process is better understood.

Practitioner or professional? Being an appraisal practitioner and a professional appraiser should be synonymous. But the current state of the profession makes the two quite distinct.

Some argue that full-time independent appraisers are the professionals and that merchants who appraise are simply dabbling with a sideline. Such a definition is nice for the independent and provides an easy answer for some of the troubling questions. But it's too easy and probably wrong, arbitrary and misleading.

David vs. Commissioner

Subject: Charging a percentage of the appraised value as an appraisal fee creates the appearance of impropriety and questions the credibility of an otherwise qualified appraiser.
Case: "[The petitioner's expert's] fee for making the appraisals was based on a percentage of the values arrived at. While we are not questioning [the appraiser's] integrity, we cannot ignore the fact that a motive existed to arrive at high values. This does not mean the percentage fee arrangement invalidates the appraisal, but rather it simply means we must view the appraisal with added caution."

– U.S. Tax Court

1976

Stone vs. Those Certain Underwriters at Lloyd's of London

Subject: Failure to disclose that the seller provided an appraisal, at the time of sale, for more than the sales price could be grounds for insurer to cancel the policy after a loss.
Case: "Did the plaintiff's failure to disclose information regarding the wide variation between purchase price and the contemporaneous appraised value and the fact that the seller and appraiser were one and the same person constitute a misrepresentation that affected the materiality of the risk and furnished grounds for recission? Justice and precedent compel an affirmative answer."

– Illinois Appellate Court, Fifth District

1980

Safeco Insurance Co. of America vs. Sharma

Subject: Appraiser as an impartial provider of information on value. Engaging in issues of authenticity exceeds an appraiser's role when serving on an insurance claims panel.
Case: "In no authority is it suggested that an appraisal panel is empowered to determine whether an insured lost what he claimed to have lost...Certainly, an insurer is free to litigate whether the insured has misrepresented what he lost, but it is beyond the scope of an appraisal."
– California Court of Appeal, Second District

1984

Regardless of whether you are a merchant-appraiser or an independent, if you're going to appraise, you should be a professional. You can be an appraiser who also sells the type of items in question or one who does not. You can limit your practice to certain types of appraisals (insurance replacement, for example). Such distinctions don't change the fact that a jeweler can be a professional appraiser or that an independent appraiser can be unprofessional.

Appraisers should not arbitrarily decide to appraise old-cut diamonds for the replacement cost of modern-cut equivalents. (Stones supplied by D. Atlas & Co. Inc., Philadelphia, Pa.)

Standards make a profession: There are many ways to define a profession and many elements that allow an occupation to be defined as a profession. A profession requires:

• Some degree of standards (a codified body of knowledge encompassing certain principles, procedures and methodology);

• Some medium of education that allows practitioners to learn the standards; and

• At some point, a collective body of practitioners who profess to subscribe to those standards.

Ideally, members of a profession can be formally educated, tested and certified in these standards; can pass on the knowledge learned to others; can promote understanding and growth of the standards; and can develop a procedure to monitor and enforce compliance with the standards.

Despite a lack of government regulation, most of the above exist today in the fragmented, voluntary profession of personal property appraising (which includes gems and jewelry). However, government regulation may be needed to induce groups to agree on one set of uniform standards. Although they shared a similar base and slowly came together on basic principles, groups involved in real estate appraisal took decades to agree on a minimal uniform standard. Federal intervention finally accomplished the task.

While we can glean some founding principles from real property appraising, personal property is different – and more difficult – to appraise, primarily because of its portability. One thing is certain: it will be difficult to convince the client community that appraising is a profession as long as those who do it maintain there are no standards and as long as each practitioner writes appraisals as he or she wishes. Remember that the courts have not considered a lack of uniform opinion sufficient reason for an appraiser to have no formal appraisal education.

Who is an appraiser? Neither the federal government nor any of the 50 states regulates appraisers of personal property. Some states are considering licensing and/or certification. But, appraisal reports and some procedures related to appraising and running an appraisal practice are subject to federal, state and municipal regulations.

There is no such thing as a "licensed appraiser" of personal property in the

TIMELINE OF SOME IMPORTANT APPRAISAL-RELATED COURT DECISIONS ON SELECTED TOPICS

Costa vs. Neimon

Subject: Appraiser has liability for negligence to a third party who the appraiser should foresee would come "within the ambit" of harm that could result from a carelessly done appraisal.
Case: "The duty of any person is to refrain from any act which will cause foreseeable harm to others, even though the nature of that harm and the identity of the harmed person or harmed interest is unknown at the time of the act.... An appraiser's failure to use due care in performing an appraisal is negligence because it is an act or omission in the face of foreseeable harm. It is not necessary that the appraiser have foreseen the harm to the particular plaintiff [the third-party buyer who relied on the appraisal]. The appraiser should have foreseen that a prospective buyer of the property being appraised was 'within the ambit' of harm which would result from a carelessly done appraisal."

– Wisconsin Court of Appeals

1985

Lio vs. Commissioner

Subject: Donation or estate tax FMV cannot be based on sales to a dealer who is buying for resale [in purchased form].
Case: "...the sale to the ultimate consumer [the 'public'] is any sale to those persons who do not hold the item for subsequent resale."

– U.S. Tax Court

1985

Price vs. Commissioner

Subject: Original cost isn't necessarily the best evidence of value.
Case: "In many cases, actual sales of property to be valued are the best evidence of fair market value.... We must also, however, consider reliable opinion testimony as to value.... The items...were sold as tourmalines although some were beryls. They were priced in bulk by average carat value. The likelihood that the price charged to petitioners was inflated is increased by petitioners' apparent lack of knowledge...Under all of these circumstances, cost is not the most reliable evidence."

– U.S. Tax Court

1985

United States. Some municipalities require appraisal practitioners to obtain a business license, but this doesn't certify any particular qualifications as an appraiser. Until a state does license personal property appraisers, however, it will be difficult to prevent a merchant with a business license from advertising as a "licensed appraiser," though some professional appraisal societies consider such practices unethical.

Many criticize the government for its Band-Aid approach of regulating individual appraisal problems rather than deal with the disease itself by regulating appraisers. However, we can borrow a page from the government and assume that to understand what an appraiser is, we first must understand what an appraisal is.

What is an appraisal? An appraisal is an opinion of value, cost estimate or analysis in a defined market. Appraisals don't exist in a vacuum. Individuals and legal entities seek appraisals for specific reasons, although we often lose sight of the most fundamental one – to serve as a basis for making some financial decision.

It's this simple: two entities want to enter into a relationship or conduct a transaction for which they need an impartial, informed judgment about the worth of an item at a specific time for a particular market level. If appraisers always remembered the purpose of an appraisal and the needs of clients and third parties, many appraisal problems would go away.

APPRAISERS do not create or influence markets. Appraisers do not set prices or establish the conditions for transactions in the marketplace. An appraiser's role is to be knowledgeable of the market and its items and to analyze prices in the market, impartially and without advocacy, to provide his or her opinion of value.

More than a decade ago, the North American Conference of Appraisal Organizations (NACAO – primarily an umbrella group of real estate appraisal organizations that reformed as the Appraisal Foundation in 1987) defined an appraisal as: "A [written] statement, independently and impartially prepared, by a qualified appraiser, setting forth an opinion of defined value, of an adequately described property, as of a specific date, and supported by the presentation and analysis of relevant market data."

That definition – since clarified, modified and expanded in personal property appraisal education programs – tells the story. *An appraisal is the opinion of an informed expert. It is prepared to provide meaningful information for the use of clients and third parties.* It explains some of the ingredients without which an appraisal simply will not serve its purpose.

Clients and third parties have every right to believe the appraiser is not an advocate for any party to the transaction or any particular position. And because of market variables, they can expect the appraiser to explain the parameters within which they can rely on the stated value. An appraisal must be based on value in a defined market, not simply on one store's low or high prices.

Appraisal ethics: A jeweler can be very moral and honest and still be considered an unethical appraiser! Appraisal ethics are not the same rules that society applies as a test of moral conduct.

A profession is concerned primarily with behavior that speaks to the professionalism of one of its own and how such behavior reflects on the profession as a whole. If a collective body of practitioners subscribes to a standard of professionalism which one violates, that individual is judged unethical. A lay person who doesn't understand why the professional is required to behave that way might feel that professional ethics contradict society's scale

Anselmo vs. Commissioner

Subject: Item must be valued as is, not as though in some other possible form (implication for appraising old-miner as modern cut). Also, donation (and estate and gift tax) FMV definition of "public" is the ultimate consumer, and the "ultimate consumer" could be a manufacturer not buying for resale in the purchased form.
Case: "[Petitioners'] appraisers estimated the retail value of a stone by calculating the portion of a [hypothetical] finished jewelry item's retail price that could be attributed to the [loose commercial quality] gem.... The commissioner's experts valued the gems on the assumption the 461 stones would be sold together to a single jewelry manufacturer or retail jeweler. The [lower] court concluded the commissioner's experts were correct.... The Anselmos contend...that the Tax Court erred by not valuing the stones as the portion of the jewelry's retail price attributable to the stones.... The most appropriate purchaser [in a federal tax FMV scenario] is not invariably the individual consumer. For example, the general buying public for live cattle would be comprised primarily of slaughterhouses rather than individual consumers. The fair market value of live cattle accordingly would be measured by the price paid at the livestock auction rather than at the supermarket."

– U.S. Court of Appeals, 11th Circuit

1985

Hecker vs. Commissioner

Subject: 1.) Court's distinction of appraiser's evaluation expertise vs. valuation expertise. 2.) Rejection of appraising by price guides and formulae in favor of knowledge of market activity.
Case: "[Petitioner's appraiser's] principal expertise is in evaluating the quality of gemstones rather than their dollar value [and thus he] was forced to value the tourmalines and mineral specimens based on nationally available pricing guides.... We were unimpressed with [his] experience and credentials... We have serious doubts that the methodology he used...yielded values that reflected market prices accurately."

– U.S. Tax Court

1987

of morality. For example, most people would say it's not immoral or dishonest to advertise. But it used to be against the American Bar Association's agreed-upon standard for lawyers to advertise. That made it unethical for lawyers. (See box below, "What I Paid is Irrelevant.")

This subject may seem esoteric, but it goes to the heart of the appraisal dilemma. Is appraising a profession whose rules consist of certain principles and procedures for the valuation of property? Or is it just an extension of a trade to be judged by each merchant's notions of morality?

The profession of personal property appraising is young and growing. Opinions abound as to the nature of the profession, its current status and its future direction. This results in a transition stage in which old self-assuring notions will be bandied about as though someone brought them down from a mountain. Much of this activity seems to center on the question of appraisal ethics. (See box, "Stop the 'Unethical' Jeweler in Our Area!" page 121.)

To judge what is and isn't ethical in appraising, we need to look at the right set of rules. Some governmental bodies have adopted minimal standards of conduct for specific types of appraisals. And a number of appraisal organizations have published ethical-conduct codes for appraisers. A cursory look at these codes reveals a consensus on at least minimum guidelines of ethical conduct. This might help a judge decide whether an appraiser acted properly in case of a dispute.

A JEWELER

can be very moral and honest and still be considered an unethical appraiser!

Codes of conduct, standards of practice, and principles and procedures of methodology are all linked in an indivisible package. Such a package has much to offer the practitioner as a guide to professional, ethical appraising.

INTRODUCTION TO PROFESSIONAL APPRAISING: THINGS TO LEARN & DECIDE

We touched earlier on what an appraisal is. Let's expand on that by looking at the meaning of value.

A single item at a certain time can have many different types of values. This often shocks clients and new practitioners. But it gets worse. There also can be many different but equally correct opinions as to what dollar amount most represents value. (See box, "Value Defined," page 122.)

It should be obvious that the value of an item can vary as facts relating to the item and the particular transaction vary. It also should be expected that the opinion of appraisers will vary even in the very same scenario.)

'WHAT I PAID IS IRRELEVANT'

It's the mid-1980s and industry concern with the appraisal dilemma is growing. People are looking for answers. A major jewelers' organization presents an interim mitigating policy for its members. "When writing insurance appraisals on items you have sold," says the organization, "the appraised value should be your selling price. What you charged is the best measure of retail value."

During the period of these debates, a customer comes into the store with an item of [new or used] jewelry he recently bought elsewhere. He asks for a "retail replacement value appraisal" to be used in obtaining a floater on his homeowner insurance policy.

In the initial client interview, the jeweler/appraiser asks when the customer bought the item, in what kind of store and how much he paid.

The sudden silence can be cut with a knife; the client tries to retain his composure and, with a knowing and familiar smirk, asks why the jeweler wants to know. "What I paid isn't relevant!" he says. "What am I paying you for? I'm not going to do your job for you! The other jeweler told me you'd try to kill their sale and I told him that wouldn't happen because I thought you were a professional appraiser!"

With that parting remark, he walks out the door before you can explain the important and valid reasons for your questions, before you can explain that the very reason you asked is that you're a professional.

Two years ago, a jewelry trade press journalist wrote an article about appraisal methodology. The reporter took a piece of jewelry to different jewelry appraisers to see how they would value it. The article told how some of the appraisers had asked what the cost was. In a recurring theme, the author appeared to accuse those who did ask of performing improperly.

Why would one jewelry organization proclaim that appraised values should be equal to the selling price while a journalist decries an appraiser asking about that selling price? Would a client believe it wrong for an appraiser to make such an inquiry if he hadn't gotten that impression from the performance of past appraisers? Why would those other appraisers have shied away from the question?

I think it's safe to say that many in the trade would think asking a client about the cost is wrong – even unethical! Yet many jewelers base their own appraised values on what they themselves charge. Aren't they judging what should be considered ethical against different sets of ethics in different situations?

Many appraisal standards seem unclear to practitioners who haven't gone through formal appraisal education and testing. The standards of many appraisal societies and some government regulations make clear that to determine the value of an item, the appraiser must take into account its recent sales history. The recent sale of an item should be treated just as he or she would consider recent sales of similar items.

I recall one trial in which an expert with many years of trade experience shocked the judge with his view on this issue. In arriving at a value, the expert relied on his own opinion and the opinion of others as to what the item *would* sell for. The item in question had been sold a short time before the valuation date in question. When the judge asked why the appraiser didn't consider this much lower recent sale, he said he would never allow himself to be biased with knowledge of such facts. The judge found against the appraiser's opinion (for many reasons).

Value vs. price: Much valuation confusion centers on the failure to distinguish between selling price (or "cost") and value. In a capitalist system (an open market free-enterprise society), the same item often sells at different prices. That's why appraisers are needed.

Within the limits of what the law expects to be "conscionable," sellers are free to compete around price levels they feel the market will bear. Conscionable or not, the price paid for an item exists as a fact in the marketplace. Value, however, is not a fact. It's an appraiser's opinion based on the facts – in other words, the prices (usually plural) paid.

When performing appraisals, merchants must be aware of their very different role as an appraiser. Appraisers do not create or influence markets. They do not set prices or establish the conditions for transactions in the marketplace. Their role is to be knowledgeable about the market and its items and to analyze prices in that market, impartially and without advocacy, in order to provide an opinion of value. Appraisers are supposed to base their opinions on knowledge of actual market activity – not on what they feel the market should be.

Undefined value = non-value: Appraisals that define value as "stated value" actually mean "we don't have any particular market or type of transaction in mind. Use this for all of your appraisal needs." This is a typical cause of the appraisal dilemma which exposes the generous appraiser to lawsuits alleging negligence.

Different types of appraisals require different types of value. Failure to identify the type of value or to restrict its use to a particular client need provides a legal document that any party can use for any purpose they wish. If used in the wrong scenario, the appraiser might be held liable for resulting damage.

Appraisers must explain this to clients. Ignoring the problem won't make it go away; an umbrella of ambiguity provides only a false sense of security.

Clients typically request jewelry appraisals for one or more of the following reasons:

- To obtain insurance.
- To confirm they paid a "fair" purchase price.
- To resell an item.

Many appraisers still allow clients to believe an appraisal for any one of these can be used for the other two. Often they do so simply by failing to say otherwise. (See box, "I Just Want to Know What it's Worth," page 123.)

Broader misconceptions are that appraisers have a primary role to evaluate (authenticate) a client's property and to make decisions for the client.

Here are examples of decisions that appraisers believe they can make without consulting the client. That an old watch in used condition should be appraised for replacement with a new watch. That an old-mine-cut diamond should be replaced with a scaled-down modern-cut equivalent. That used or old jewelry should be cleaned, that the diamond in a new ring should be removed for grading and that the only market a client should consider for resale is "dumping to the trade."

STOP THE 'UNETHICAL' JEWELER IN OUR AREA!

"There is this one jeweler in our area who is really unethical. What can we do to stop him?"

I've received many telephone calls like this during the 15 years I've been involved with appraisal organizations. In almost every instance, the jeweler seemed honest and sincere in believing the other jeweler was unethical and should be stopped from fostering a bad image for all jewelers.

"What do you want me to do about it?" I would usually ask.

The jeweler's typical response: "I was hoping you could bring some action against this jeweler appraiser."

I would suggest writing a letter to the jeweler in question, but warned it probably would do little good unless that jeweler was a member of our appraisal organization. I also would suggest the caller contact the Jewelers Vigilance Committee.

Typically, the caller would ask for a written code of ethics or standards so he or she could refer to it in a complaint about the "unethical" jeweler to the city attorney or state attorney general.

"Sure," I would respond. "I'd be happy to send you a copy of the relevant ethical code or professional practices standard along with a letter explaining its application to your particular complaint.

"But, if you don't mind my asking," I would add, "do you do appraisals?

The typical response: "Only for insurance and an occasional estate appraisal."

I would ask to what standard the caller performed appraisals and to which code of ethical conduct he or she subscribed.

"Oh, we haven't taken any course or appraisal test, if that's what you mean," the caller would say. "But we've been jewelers for X years, we have two gemologists on staff and we read all the appraisal books and articles that come out from time to time."

What's wrong with this picture? "OK," I would say. "Let's say I send you our code and you take your complaint to the attorney general. You lay out the activity of this other jeweler and you present our standard as proof of his/her 'unethical' conduct. How would you handle the following possible scenario?"

Then we'd play out a possible meeting with a city attorney or state attorney general (AG) and a group of jewelers initiating the complaint (CJs):

AG: "We might be able to use the appraisal 'standards' you've provided. But an important factor might be what the law calls 'traditions and practices in the trade.' So let me ask whether most of the jewelers in your area write appraisals?"

CJs: "Yes."

AG: "Good, we can use that to show this other jeweler is not following accepted standards. Now this is very important: do all or most of you follow the appraisal standards you've given me when you write appraisals? Or are there significant parts of this standard that some or most of you do not subscribe to?"

CJs: "Well, we don't belong to that organization and haven't taken its courses so it would be hard to say. We're not really familiar with all of that standard..."

Something is wrong with this picture! To say that some appraisal activity or procedure is or is not ethical requires an accepted standard as a mirror to which the activity can be compared.

In reality, an appraiser's primary role is simply to provide information on an item's value. Clients should be told about choices such as those just listed and also told the report will include any limitations related to such areas. But it's up to the client to decide how to proceed.

1.50-ct. old-miner cut = 1.20-ct. modern cut: The notion that old-cut diamonds should arbitrarily be appraised for the replacement cost of modern-cut equivalents is a prime example of decisions an appraiser should not make.

First, it's the client's choice whether to replace with a similar "old" item or a "modern" equivalent.

Second, market reality shows that old-cut value simply is not equal to modern-cut value.

Third, if a client wants a 1.50-ct. G VS_1 old-cut diamond replaced with a modern equivalent, the equivalent is a 1.50-ct. G VS_1 modern-cut diamond, not a 1.20-ct. G VS_1 modern "equivalent!"

This example shows why appraisal methodology should be based on a knowledge of appraisal principles, not just on gemological training or trade experience alone. (See box, "The Big 'E' in E-Valuation," page 124.)

It's beyond the scope of this article to debate whether someone must be a gemologist to appraise gemstones or a metallurgist to appraise jewelry. But it's clear that an appraiser should obtain as much product knowledge and market information as possible. It's also clear there's a wide universe of knowledge called for in appraising the multitude of gem and jewelry items.

This article proposes:

- That knowledge of appraisal principles and methodology is an absolute must for appraising.
- That applying this knowledge to each appraisal depends on the needs

VALUE DEFINED

A full discussion of the many values an appraiser must consider is far beyond the scope of this article, but we can look at some introductory basics.

Value is the best and impartial opinion of an appraiser as to a dollar amount that is most representative of the fair range of prices typically paid for an item.

For value to have meaning, it must be attached to a particular set of facts, including the quality and condition of the item, the market and/or market level where relevant transactions take place, the position (or desirability) of the item in that market and at a particular time.

Market value generally is intended as a guide to the types of transactions an appraiser is to consider as the basis for forming an opinion of value. The component elements – which are designed to weed out transactions that are extraordinary to the market – are:

- An arm's-length transaction in a free and open market subject to all normal market influences, specifically no private (secret) sales or sales between parties with special relationships.
- Sales between the greatest number of buyers and sellers who are:
  - – Reasonably well-informed of the facts related to the item and its position in the market.
  - – Willing to buy or sell but under no particular compulsion to do so.
  - – Entering the market in a time frame that would be considered normal and reasonable for sellers and buyers in that market or market level.
  - – Acting prudently and in their own best interest regarding the value of the property (or transaction).
  - – Typical in their motivation for buyers and sellers normally expected to be transacting business in the relevant market or market level.
- Sales in which payment is:
  - – In the form of cash or some measurable and consistently definable equivalent.
  - – Financed, if such financing is typically the method of conducting business for the property in the market and on terms generally available to buyers at the time relevant to the valuation date.
  - – For the item itself and does not include any atypical add-ons of goods and/or services or special incentives to buy.
- Proper reconciliation and adjustments for atypical forms of payment or for special transaction conditions.

Market value tells an appraiser how to look at transactions and what kind of buyers and sellers to consider. What it usually doesn't do is define the particular market or market level in which the appraiser is supposed to be looking. The assignment does that.

Often, the item itself, the agreed-upon needs of the client and third party or government regulations select the market to be used for market value.

Fair market value or FMV is probably the most misunderstood and misapplied term in the world of appraising! It's usually a legal term that has been defined for the needs of a particular legal "jurisdiction." In this context, jurisdiction can refer to a court, a level or branch of government, and an administrative or regulatory agency.

Most dangerous are the notions that there is a single definition of FMV and that any one definition can be applied arbitrarily to any assignment in which someone wants the fair market value. Law dictionaries do define FMV, but these definitions usually just combine some of the generic elements of "market value."

Individual state or federal agencies typically take these elements and modify or restrict them for application in a particular type of market, perhaps by designating a market level (applicable buyers and sellers) or geographic region to be used in arriving at FMV.

Insurance often confuses practitioners and leads merchants to proceed with all appraisals as though the item were being replaced. A look at the elements of value outlined above should clarify that replacement value (cost) is not a jumping-off point for other appraisal values.

In the strictest sense, replacement value is a major exception to "normal" value. In insurance, the issue often is compensation or the ability to replace rather than value. Usually, an insured person and the insurer sign a contract (policy) in which they agree on a method of making the insured whole and/or on a number to be the basis of compensation in the event of a loss. Insurance companies often accept the buyer's cost or selling price as "value" without any appraisal. However, this approach can change drastically in the event of a dispute following a loss, depending on the language in individual insurance policies.

presented by the item in question and on the needs of the known client and of any foreseeable third party.

• That clients should decide on any options that are theirs to decide.

Take-in: It should be apparent by now that many problems can be resolved at take-in – the time for the critical initial client interview. Widespread gemological training has taught many jewelers the limitations that should be placed on gemstone identification during take-in for cleaning, repairs, modifications and appraising.

Ideally, the appraiser should handle jewelry taken in for appraisal. However, other staff members with fundamental appraising knowledge can handle the basics, perhaps avoiding a final commitment on the scope and fee until the appraiser can speak with the client.

Which services? In deciding to offer appraisals, the jeweler needs to decide on the scope of appraisal services and the background of personnel who will provide them. There are many options to consider.

Which items to appraise

• Only new or old items that you have sold.

• Only new or old items the client acquired elsewhere.

• All of the above or only certain types and categories of gems and jewelry (or of silver, coins, watches, decorative arts, etc.).

Services to be offered

• Basic appraisal (valuation) service.

• Evaluation (gemological) service.

• Full evaluation/valuation (gemological appraisal) service.

Types of appraisals

• Insurance for new, used and/or comparable items.

• Standard consumer services (insurance, confirmation of "fair" purchase price and consumer resale).

• Services for the professional client community. (Note: This category can be very lucrative and attract a new client/customer base, but it also requires more advanced appraisal background and proficiency.) It includes:

– Insurance damage and claims appraisals.

– Divorce, state probate, bankruptcy, etc.

– Federal tax-related appraisals for estate tax, taxable gifts, charitable contribution deductions, IRS seizure of property, etc.

– Miscellaneous government-related appraisals for the postal service, law enforcement agencies, FDIC/RTC, etc.

– Appraiser expert witness and/or trial consultant services on any of the above.

Options if not offering appraisals

What if you don't offer any appraisal services? You still need to:

• Obtain and maintain fundamental knowledge of the professional appraisal process that still affects you.

• Avoid unconditional "Guarantees of Appraised Value" on items you have sold – a traditional but risky procedure considering the current state of the profession. If you provide such assurance at the point of sale, consult your attorney on how to make the "guarantee" conditional on the background of the appraiser and the type of appraisal obtained.

• Embrace one of the new breed of independent appraisers practicing in

'I JUST WANT TO KNOW WHAT IT'S WORTH'

Some appraisal clients so distrust jewelers/appraisers that they believe explaining why they want an appraisal somehow would bias the result.

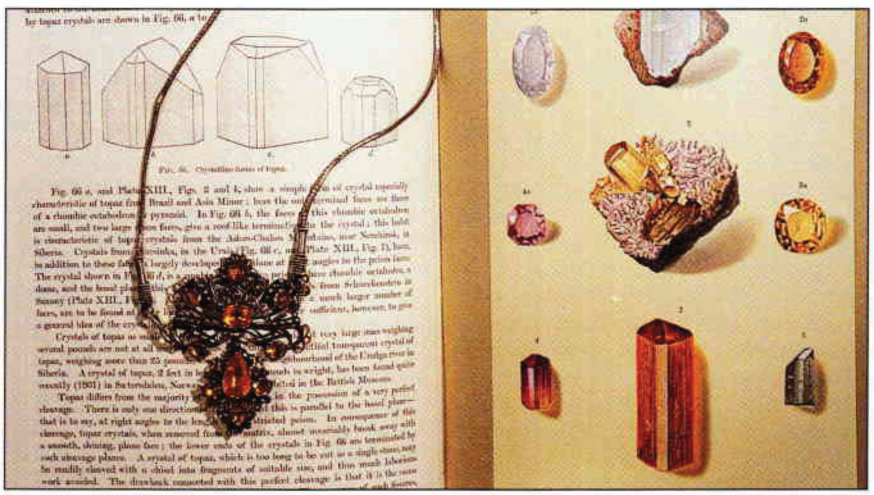
Having been told by the seller that other jewelers will try to "kill the sale" with a biased appraisal, clients often misstate the real reason for an appraisal or the history of the item. They often will insist that the reason for the appraisal doesn't matter and that they "just want to know what it's worth."

The first thing to clarify is that an item can have many values; which one applies should be defined in the report. You also should explain at the start that the intended use dictates the type of report format to be used, the market level to be examined and the type of transactions selected for comparison, not just the type of value.

Clients should be told the report will be limited to its stated use. It might contain language such as: "'Retail Replacement Cost Estimate – New' stated herein has been provided to assist the client in obtaining insurance for items of like kind and quality in new condition. This report and its stated value(s) are valid for this use only and are invalid for any other use, including, but not limited to, 'consumer resale' or 'confirmation of fair purchase price.'"

It's beyond the scope of this article to explain the differences between these values. However, these are the typical client appraisal needs that many people erroneously believe can be addressed by an appraisal for any one of them.

A paragraph such as the one above should limit any appraisal to just one of these uses. (There are multivalue, multiuse appraisals, but that's another story.)



Education is the key to proper appraising, but that education must provide far more than just knowledge of gems and jewelry.

your community. Such a non-selling, or limited-selling appraiser can keep your customers from going to another jeweler who does provide appraisals.

• In place of an "appraisal" at the point-of-sale, consider providing your customer with a "Statement (or Estimate) of Replacement Cost in Our Store." This is not an appraisal, but rather a restatement of your selling price, and can be on a form or your own stationery. I have taught and published the concept since 1984, and it is beginning to take hold as an accepted industry procedure. It might also be called, perhaps more properly, "Insurance Replacement Estimate."

You also might consider loose or formal ties with professional appraisers specializing in other types of personal property such as antiques, silver, fine or decorative arts and collectibles, machinery and equipment and even real estate. This gives you access to diverse research sources and information-sharing. In addition, the more lucrative professional appraisal assignments often call for a team of appraisers in a number of specialties. Such could be the case with divorce, estate, tax, liquidation and many other types of appraisals. Often, an appraiser in one specialty contacts one in another specialty for help. It pays to be in the circle.

Background and qualifications: The type and scope of appraisal services you offer affect the training and experience you or your appraiser should have. Background in appraising should include:

• Appraisal education, testing and certification.

• Appraisal experience and/or internship (formal appraisal internship is a relatively new concept).

• Prior experience with specific types of appraisals.

• Knowledge of government regulations relevant to the types of appraisals you offer (also the ability to research and keep up with new and modified regulations).

Background in the jewelry trade should include:

• General trade experience and involvement and/or apprenticeship.

• Gemological and/or other product knowledge education, testing and certification.

• Access to and working knowledge of relevant instrumentation and outside laboratories.

• Experience and/or education related to jewelry arts, fabrication and/or repair techniques.

• Knowledge and background specific to the categories of items to be appraised.

In addition, the appraiser should have access to a library of appraisal texts and maintain an ongoing appraisal education program. Education and experience as a witness/trial consultant will be needed if that's relevant to your practice.

Today, jewelers who appraise have a golden opportunity not available just 15 years ago. Now they can reap the benefits and profits of being part of a profession. If you are going to appraise, make the commitment to really be an appraiser. If you offer appraisal services, be sure you offer nothing less than *professional* appraisal services. Only then will the profits outweigh the pitfalls.

THE BIG 'E' IN E-VALUATION

While the process of valuation can, and often should, include evaluation, the relationship between the two seem to have gone topsy-turvy.

An appraiser's primary role is to provide information on the worth of an item. Depending on the type of appraisal or the defined needs of a known client and a foreseeable third party, varying levels of evaluation might also be required.

These two terms usually are considered synonymous, but have important distinctions in professional appraisal terminology. A "valuation report" is mainly a vehicle to convey a defined opinion of value (monetary worth); an "evaluation report" offers broader information. Most appraisal valuation reports include some evaluation information. An evaluation report may or may not also include an appraiser's estimate of value.

Evaluation could consist of:

• Identifying and (possibly in-depth) grading of materials.

• Authenticating the background or origin of an item.

• Proposed changes to an item.

• Analysis of available markets for client buying or selling activity.

It is not necessarily the appraiser's role to provide all this information for every item in every appraisal report. Nor should he or she automatically do so and bill the client for the cost. That is for the client to decide after being informed of the options, the pros and cons, possible results, costs, etc.

A classic case involves the question of whether a diamond can be appraised in the setting. Of course it can! To say that a diamond must be removed to be graded (evaluated) for an appraisal is to say that many types and sizes of gem-set jewelry can't be appraised.

The industry deals with gray areas like this by issuing conflicting proclamations of what must always (or never) be done. But there's no need to select an arbitrary extreme. The issue is not whether to do it or not. Instead, the issue is how and when to do it and how to be clear in the report just what was or was not done and why. Like many appraisal questions, it involves report-writing more than procedures.

Similar considerations go into deciding when to use gemological or metallurgical procedures to identify component parts of an item or authenticity procedures to establish its background.

Appraisals often are based on readily apparent identity. This limited valuation procedure must be appropriate for the assignment, and any parties who may rely on the report must know the limitations. (Don't use "readily apparent identity" to run amok with appraising items you don't understand; you might have to justify the background and basis of such a call as well.)

Bottom line: the amount and cost of evaluation procedures to be included in an appraisal assignment usually should be the client's decision and not the appraiser's.

IF YOU WANT

to take this quiz, fill in the answers, photocopy your reply and send it with your name, store name and address to "JCK Management Study Center, 1 Chilton Way, Radnor, Pa. 19089." Replies to the current test should be postmarked no later than Nov. 15, 1994.

To take an updated version of the quiz - email: AiCertify @gmail.com for availability