

FORMS AND EFFECTIVENESS OF THE CLIENT'S INFLUENCE ON THE MARKET VALUE OF PROPERTY - CASE STUDY

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Abstract

Although real estate valuation is supposed to make the market transparent, it has been noted to be partial in many countries. Analysis of literature and results of the statistical analysis of survey responses of Polish property appraisers indicated that: Property valuers operate in an environment which exerts influence on the final result of valuation. The attempts of the client to influence the valuation process and their effectiveness do not depend on the gender and age of the property appraiser. The problem of valuation bias should be seen in the weakness of the system enforcing compliance with ethical standards, with this being an area which requires reinforcement in many countries.

Key words: *client behaviour, real estate appraisal, valuation partiality.*

JEL Classification: *D80, D81, L85, R39.*

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1. Introduction

The property market attracts huge capital. Globally, investments in 2017 were estimated at 1,390 billion USD (CUSHMAN & WAKEFIELD 2017). When making investment decisions, market players need to know the value of property and therefore require professional valuation.

Internationally, property valuation is defined as the process of determining value but also as the result of that process. Most valuation purposes require determining a value that will objectivize the market. Only objectively determined value guarantees secure and reasonable management of property and the sense of social justice (ŻRÓBEK et al. 2014).

Unfortunately, no attempt at determining the value of property or goods is free from subjectivism. It turns out that the interaction between market players merely reduces subjectivism, rather than eliminating it (HAVARD 2001; BRZEZICKA 2016; ŻRÓBEK-RÓŻAŃSKA 2016).

Incomplete objectivity results primarily from a given researcher having to evaluate the researched subject and, secondly, from the approach of the researcher. Application of the observation method

carries a risk of superficiality and partiality of observations. Research shows that cognitive processes rely on mental construction of images and events that are the result of the interpretation and inference of received stimuli; perception and objective reality are incongruent (PISKORZ, ZALEŚKIEWICZ 2003 pp. 116-118). This means that determining the value of any property or good involves uncertainty and entails risk. Value uncertainty seems to be particularly high in the property market. Although the property valuation process has now been considerably normalized, valuation results are still not free of subjectivism nor the influence of other parties, including the clients.

2. Motivation behind the research

So far, researchers and practitioners have been focused mainly on the most sought-after value, i.e. market value¹, which is defined in the International Valuation Standards (IVS, 2017) and European Valuation Standards (EVS, 2016) as follows:

Market value is the estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.

Research on the value determining process has been clearly evolving. Initially, it focused on the methodology and accuracy of valuation, with the focus subsequently shifting to the valuation process itself in order to analyze the stages of determining value. While studying the accuracy of valuation, it was noted that valuation, which is supposed to reflect the market, failed to keep up with it, frequently leading to overestimation or underestimation.

This being the case, research is now focused on looking for the causes of this flaw. It was investigated whether the problem was in the actual nature of property valuation, in the valuation procedure, in the behaviour of valuers, or in the professional environment that the valuers work in (KUCHARSKA-STASIAK, ŻRÓBEK 2015). It was noted that the property market was influenced by a number of non-economic factors, including social, cultural, and psychological ones, to a higher degree than other markets. Also, the research was affected by a lack of information sufficient for the proper analysis of the market.

A particularly fruitful area for research was the behaviour of property valuers and the professional environment that they operate in. These people also operate in an environment which exerts influence on the final result of valuation, meaning that there is a genuine risk that valuation may be compromised as a result of interference from clients (ordering parties of valuation reports), and also as a result of the conduct of the valuers themselves. A thesis of bias in valuation was advanced, which is in contradiction with the fundamental requirements of international and European valuation standards (EVS 2016, 2017), standards of the Royal Institution of Chartered Surveyors (RICS 2017 p. 23), as well as with the European Union directive (DIRECTIVE ... 2006). All of these regulations attach great importance to the impartiality of valuation.

The above prove that the issues covered in this article are extremely important, not only for the recipients of valuation, including investors, actively involved in the property market, but also for valuers, who bear professional, legal, or even criminal responsibility. They should be provided with a proper theoretical foundation. This demonstrates the validity of research into behavioral aspects of valuation on many national property markets.

3. Aim of the study and adopted research methods

The aim of this paper is twofold: (1) to correlate direct and indirect causes of bias in property valuation with special emphasis on the Valuer-Client relationship, and (2) to verify them empirically using Poland, a country of lower market transparency, as an example.

The research and analysis were performed for the thesis: *The process of property valuation is burdened not only with a large dose of subjectivity, but also with partiality.* The authors decided to verify the research hypothesis that: *An important source of valuation bias are unethical client-appraiser relations.*

Pursuit of the first aim relied on broad analysis of literature on property valuation and appraisal in the economic context. In order to find the actual client-valuer relationship, a survey was conducted among Polish property valuers. Statistical tests and models, including logistical regression, were applied in the analysis of the survey responses. The results should be sufficient for showing the

¹ A survey in 2015 among Polish valuers indicated that market value is determined in 88% of all valuations (ŻRÓBEK et al. 2016).

pertinence of the existence of bias in property valuation in Poland. As such, it may prove useful for designing actions aimed at the elimination of unethical conduct in property valuation and in business in general.

4. Value objectivization and bias in real estate valuation in literature

Objectivization in the property market seems particularly difficult (KUCHARSKA-STASIAK 2013). This is so for a number of reasons – those related to the features of a property, e.g. uniqueness (no two properties are identical), its complex nature (land, buildings, but also rights and entitlements related to ownership) and immobility (a particular location), as well as those related to the features of the property market, e.g. non-uniformity (high market segmentation), a particularly high level of market imperfection, and low market efficiency. The more individual features a property (as a physical and legal entity) shows, the lower the market activity, the lower its transparency, and the less mature the market is – the more difficult the process of objectivization (RATTERMANN et al. 2014; ŠUBIC-KOVAČ, RAKAR 2008). Regardless of the level of property market development, the client is charged for the subjective interpretation of objective scientific analysis and calculations (GILBERTSON 2000; FRENCH, GABRIELLI 2003).

The main cause of such differences is uncertainty of the input data. Comparative methods adopted by valuers all over the world rely on the subjective selecting, from a set of properties, of those which the valuer deems comparable to the property being valued (REE, HAYWARD 2000; YEUNG 2014; DOSZYŃ, GNAT 2017). However, it must be noted that “objective”, acceptable subjectivism must not mean complete discretion on the part of the valuer as to making and interpreting valuation assumption and signals from the property market environment or, all the more, from particular players on that market – valuation recipients, i.e. the property valuer’s clients.

In order to prevent inaccurate, impartial, i.e., dishonest valuation reflecting their recipients’ expectations, professional organizations of property valuers in many countries develop their own codes of professional conduct. It was soon noticed that the source of behavioural aspects of a valuation process were both the client and the valuer, who is under the influence of the client (DIAZ, HANSZ 2000; KISHORE 2004; WOLVERTON 2000). In academic texts the term “influence” has a dual meaning. It may denote “pressure” but also “linkage” between market players (ACHU 2013 p. 25). “Pressure” refers to direct influence, whereas “links” refer to indirect influence on the valuer’s opinion regarding the determined value. Influence may take various forms: persuasion, suggestions, data manipulation, threats of loss of future orders, refusal to pay or reduction of pay, or even assault.

In conclusion, the behavioural research into property valuation revealed evidence of the occurrence of feedback – the clients may choose valuers that are receptive to their suggestions and put pressure on them, while the valuers may be prepared to adjust the final valuation in order to satisfy the clients’ expectations. They may be aware of unethical conduct but do it regardless in order to survive on the market or gain a higher fee. The lower the compliance with professional ethical norms, the higher the influence of the valuer-client relationship on the process and results of valuation.

To sum up the review of the relevant literature, the following can be identified as potential sources of influence, or “influence channels” leading to bias in valuation: the client and the environment where both parties operate (the market, business culture, including regulations on valuation) – see Figure 1.

Identification of potential sources of bias shows that the Valuer-Client relationship can be complex and thus difficult to detect with regard to the frequency and strength each of them has on the distortion of the determined value of the property. The forms of this influence and their effectiveness are the subject of further sections of this article, which also make use of empirical data on the valuer-client relationship in Poland.

5. Institutional determinants of property valuation in Poland

Objective determination of the market value of a property in a free market society requires the property valuer to have specific, interdisciplinary knowledge of legal, technical, micro- and macroeconomic issues influencing the price at which a hypothetical, average buyer is prepared to buy the valued property. It is common that, in many countries, including Poland, such value may legally be determined exclusively by individuals having interdisciplinary training covering technical, economic, and legal aspects of a property.

In Poland, a prospective property valuer's knowledge must be confirmed through qualification proceedings conducted by state agencies (THE ACT ... 1997; REGULATION OF THE COUNCIL ... 2004).

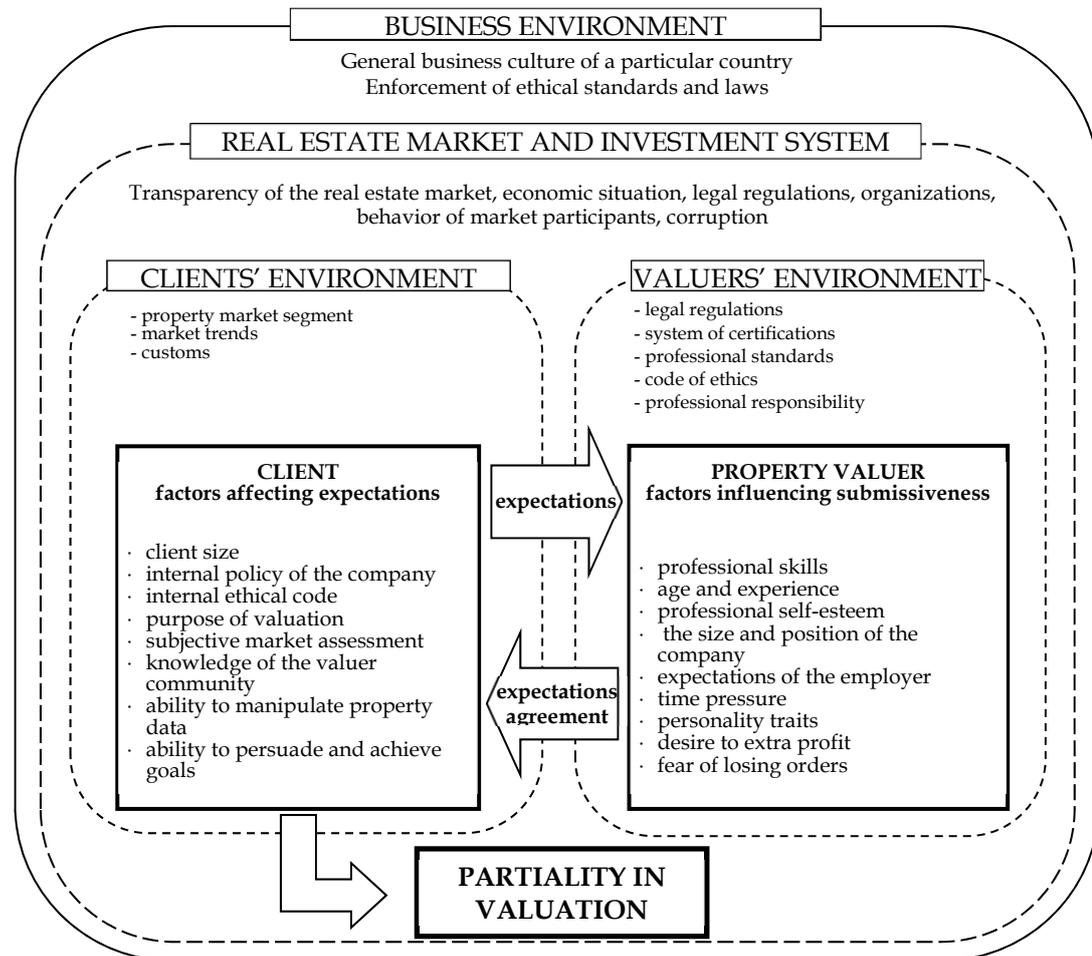


Fig. 1. Environment and potential sources of partiality in property valuation. *Source:* own study.

The central register of property valuers contains approximately 7,000 entries. They are persons holding the professional licence, including those deceased and those who do not practise the profession despite holding the licence. The number of valuers in professional associations is approximately 3,500. This figure may be assumed as the number of practising valuers providing property valuations for a variety of clients. The assumption is also based on the fact that property valuation is not the major source of income to a considerable number of valuers, since they include university teachers, civil engineers, surveyors, etc. For about half of the qualified valuers, the profession is their core business.

Practice indicates that property valuers' work is frequently criticised by the recipients of valuations, as proved by the appeals made to the Arbitration Committee of Polish Federation of Property Valuers Associations, to the performance review committees of the local associations, and to the Committee of Professional Responsibility². This naturally provokes inquisition as to whether the problem of proper value determination lies in the property value itself, in the valuation procedure, in the valuers' conduct, or in the environment the valuers operate in.

Hence, the subject of the research was the extent of the phenomenon and the circumstances of betraying the ethics of the profession of a property valuer.

² The Committee of Professional Responsibility is established by the Minister of Infrastructure and Development. It considers complaints about valuers' professional misconduct. At the Committee's request the Minister may give a valuer a reprimand, a warning or suspend or revoke the licence. In the event of being deprived of the licence, the valuer must take the exam again.

6. Empirical research and discussion of the results

6.1. Summary statistics of respondents

In order to study the extent and strength of relationships between property valuers and their clients influencing the property valuation process, the valuers were requested to take part in a written survey. It included both closed-ended questions and a number of open-ended questions. Most of the questionnaires were mailed to the members of local professional associations. Unfortunately, a mere 247 completed questionnaires were returned, which makes for slightly more than 7% of the membership. The upside of this is the fact that, on account of continuing their professional development through in-service training, the respondents had intimate knowledge of valuation issues and gave their answers consciously. Table 1 shows selected data on the respondents.

Table 1

Summary statistics of respondents

Attribute	Characteristic	%
Gender	male	51.8%
	female	48.2%
Age	< 30	9.8%
	30-45	35.0%
	45-60	24.8%
	60 <	30.3%
Education	sciences	60.7%
	economics	19.4%
	sciences and economics	6.5%
	law	9.7%
	other	3.7%
Legal status	self-employed	82.1%
	civil contract	7.9%
	employment contract	5.4%
	partnership	4.6%
Professional experience	< 3 years	20.2%
	4-7 years	11.6%
	8-11 years	8.7%
	12 years <	59.5%
Average number of valuations annually	< 10	12.3%
	11-30	15.9%
	31-50	21.7%
	50 <	50.0%

Source: own research.

The data in Table 1 indicates that the respondents are experienced self-employed valuers performing, on average, over 50 valuations per year. Most of them have degrees in engineering and are aged 30-45 or over 60.

6.2. Influence of the client on the valuation process and valuation result

As many as 90% of the respondents declared to have experienced a situation where the client attempted to influence the valuation process. However, the valuation process involves a large number of elements, such as identification of the problem, collection of source data, determination of the legal status and selection of appropriate methodology, not to mention the actual calculations. Clients tend to be interested in the final result of valuation, so it may be assumed that their attempts to interfere with the valuation process are focused on the adopted methodology and the detailed calculations that lead to the determination of value. The determined value within the same economic category (e.g. market value) should not depend on the adopted type of valuation, at least in theory. Each method of

valuation, however, requires a slightly different approach to collecting the data and the scope of market analysis. This may apply to the selection of comparable properties in the comparative approach, or to assumptions on the return rate in the income approach. Client's expectations as to the valuation result are at odds with the attitude of the valuer, who is responsible for honest and objective valuation. The behavioral factor indicating susceptibility to accepting suggestions or giving in to pressure is at play here. Over 65% of the respondents ruled out changing the result of valuation if they were asked to by the client, while a third of them declared to be willing to do so occasionally.

It was also found that clients attempted to influence the valuation process (over 80% of the respondents) more frequently than they attempted to have the determined value changed (ca. 70% of the respondents). Half of the respondents had their valuation process effectively influenced by the client. If the client's interference was effective, it usually concerned adjusting the already determined value or it occurred at the stage of arriving at the final result. Most cases concerned increasing the value of the property. Interference with the methodology of valuation was found to have been effective in a few cases (Figure 2).

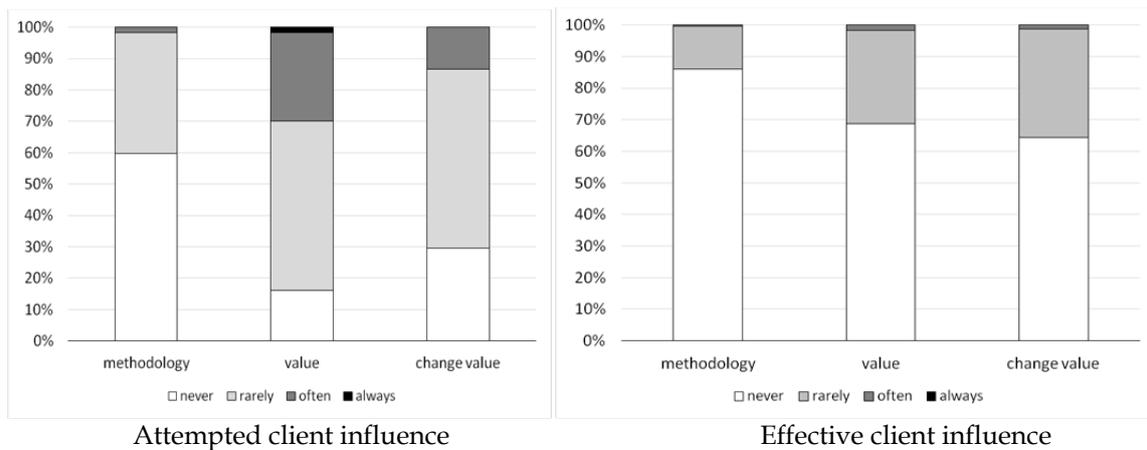


Fig. 2. Attempted and effective client influence over methodology, value, and changing the already determined value. *Source:* own study.

Effective client influence on the valuation process may result primarily from the fact that, in an under-developed property market, interpretation of its phenomena is ambiguous. This is especially the case where application of quantitative market analysis, which could help in the objective evaluation of trends and relationships, is not possible. The effectiveness of influence may also depend on the valuer's concern over the possible loss of the client (declared by ca. 20% of the respondents).

When conducting the research, it was hypothesised that the gender, age, and experience of the property valuer may have an influence over clients' attempted interference and its effectiveness. The hypothesis was verified with the chi-square test (KUMAR, SHARMA 2016). In case of the gender of the valuer, there is generally no basis for disproving the hypothesis of a significant relation (Table 2). There is, however, a minor relation ($p = 0.07$) between the gender and the number of cases where the client effectively influenced the result of valuation, suggesting that females are slightly less receptive to the client's influence.

Table 2

Valuer's gender and client influence

Attempted client influence on the valuation result					
gender	no	yes			
male	10 (8.0%)	114 (91.9%)	Chi-square test $\chi^2 = 0.35$ $p = 0.5549$		
female	12 (10.3%)	105 (89.7%)			
Tendency to change the result of valuation					
gender	never	rarely	often	always	Chi-square test
male	74 (66.1%)	36 (32.1%)	2 (1.8%)	0 (0.0%)	$\chi^2 = 2.02$

female	65 (64.4%)	36 (35.6%)	0 (0.0%)	0 (0.0%)	p = 0.2482
Effective client influence on the valuation result					
gender	no	yes			
male	56 (44.1%)	71 (55.9%)	Chi-square test $\chi^2 = 3.18$ p = 0.0747		
female	66 (55.5%)	53 (44.5%)			

Source: own research.

The detailed analysis involving the age and experience of valuers did not confirm the hypothesis. The answers are equally spread over each of the surveyed groups.

Among the forms of client influence over the valuation process, pressure or explicit suggestion can be distinguished. The survey results show that suggestions are more frequent (Figure 3).

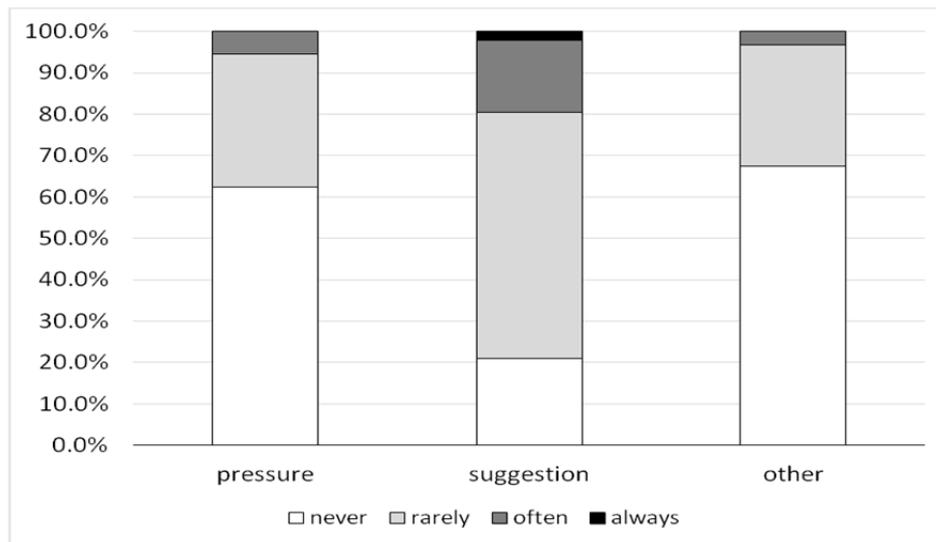


Fig. 3. Forms of client's influence on the property valuer (own study).

No statistically significant relation between the gender, age and the form of pressure was found, although the analysis results may indicate that valuers aged under 30 face pressure slightly more frequently than the older ones, aged over 60. Where the client wanted to influence the result of valuation, the range of expected change rarely exceeded 10% and concerned decreasing the value.

The research also included an attempt to determine collective significance of personal attributes of property valuers for the effective client influence on the valuation process. For this purpose, logistic regression was applied, where the response variable was the result of the occurrence of effective influence on the valuation process. The explanatory variables were the gender, age, experience and professional activity of the valuer.

A simple linear model was adopted (FREEDMAN 2009):

$$Y = \beta_0 + \sum_{i=1}^k \beta_i X_i + \varepsilon \tag{1}$$

where Y is the response variable (in binary form), X_i are the explanatory variables, β_0 and β_i are the model parameters, while ε is the random parameter. Table 3 shows the variables used in the analysis.

Table 3

Variables used in the logistic model

variable	description
Y	situation where the client effectively influences the valuation process: 1 - yes, 0 - no
X_1	gender: 0 - female, 1 - male
X_2	age: 4 - over 60, 3 - 45-60, 2 - 30-45, 1 - under 30
X_3	Professional experience: 4 - 12 years and more, 3 - 8-11 years, 2 - 4-7 years, 1 - up to 3 years
X_4	Professional activity (average number of valuations annually): 4 - over 50, 3 - 31-50,

2 – 11-30, 1-10

Source: own research.

In this model, the response variable is modelled as the logit of the probability (FREEDMAN 2009) that, in this case, a given valuer will have his valuation processed effectively influenced by the client:

$$Y = \text{logit}(p) = \ln \frac{p}{1-p}, \text{ hence } p = \frac{1}{1 + e^{-\text{logit}(p)}} \quad (2)$$

The regression results are shown in Table 4.

Table 4

Results of the logistic regression model

	B	std. err. β	p-value	χ^2 Wald	Exp(β)
gender	0.515	0.283	0.070	3.313	1.674
age	-0.099	0.211	0.640	0.219	0.906
professional experience	0.039	0.172	0.819	0.052	1.040
professional activity	0.501	0.139	<0.001	12.920	1.650
constant	-1.599	0.586	0.007	7.440	0.202

Source: own study.

Out of the analyzed variables, only the valuers' professional activity was found to be statistically significant, at a level of significance lower than 0.05. The odds ratio for the variable unit is 1.65 in this case and 4.49 for the entire range, which means that the most active valuers give in to the client's influence almost 5 times more frequently. This can be explained by the fact that as they perform more valuations, dealing with a larger number of clients, and therefore their exposure to a larger number of influence attempts is higher. The gender variable has little influence on the odds of effective influence (the significance level was 0.07) meaning that it is slightly more frequent for males to have their valuation effectively influenced by the client. However, there is no evidence to disprove the hypothesis of no influence of the age and professional experience variables.

6.3. Characteristics of clients influencing valuation process

The survey included a question about the frequency of various forms of influence exerted on the property valuer according to the client category: banks, rural communities, tax offices, developers, investors, and natural persons. Out of these, it was the natural persons that attempted to interfere with the valuation process most frequently (Figure 4).

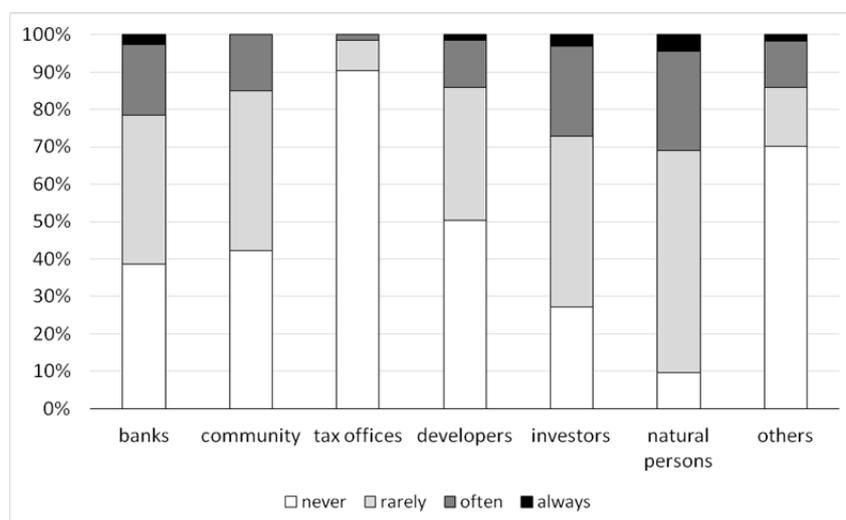


Fig. 4. Client category and their influence on property valuer. Source: own study.

The second-ranking category of clients exerting pressure on valuers are investors, where pressure occurs very often or always in 30% of cases. In the case of banks and rural communities, attempted pressure occurred in ca. 20% of cases. The least influence came from tax offices (below 10% of cases).

6.4. Purpose of valuation and client interference

Client interference, or attempted client interference, may vary depending on the purpose of the valuation. One of the most common valuation purposes is debt security. A mere less than 15% of the respondents stated they had never experienced attempts to interfere with the valuation result, while almost 40% said interference occurred either often or always (Table 5). This probably results from the fact the client was a loan borrower interested in a high value of the property used as mortgage loan security.

Table 5

Client interference in relation to the purpose of valuation

purpose of valuation	never	rarely	often	always
loan security	29 (14.6%)	96 (48.5%)	64 (32.3%)	9 (4.5%)
sale	61 (37.4%)	76 (46.6%)	25 (15.3%)	1 (0.6%)
planning fee	84 (59.2%)	38 (26.8%)	14 (9.8%)	6 (4.2%)
betterment fee	80 (57.1%)	41 (29.3%)	14 (10.0%)	5 (3.6%)
expropriation	69 (43.7%)	52 (32.9%)	29 (18.3%)	8 (5.1%)
other	41 (60.3%)	16 (23.5%)	10 (14.7%)	1 (1.5%)

Source: own research.

The fewest cases of client interference occurred in valuation for planning fee or betterment levy purposes, where almost 60% of the valuers never experienced interference. The reason may be the fact that the clients, in these cases, are local authorities. On the other hand, there were cases of property owners "soliciting" for the lowest possible value of their property. It is worth noting that slightly more respondents stated that, where influence on the value was effective, it regarded increasing the value (ca. 60%), not decreasing it (ca. 40%).

Client influence on the determined value may potentially depend on the purpose of valuation. The responses given mainly mentioned commercial and residential properties (Table 6).

Table 6

Client influence on value according to types of property

property type	never	rarely	often	always
large commercial real estate	65 (38.7%)	78 (46.4 %)	24 (14.3 %)	1 (0.6 %)
commercial premises	69 (46.0 %)	63 (42.0 %)	17 (11.3 %)	1 (0.7 %)
tenement houses	76 (48.4 %)	69 (43.9 %)	12 (7.7 %)	0 (0.0 %)
apartments	58 (33.9 %)	84 (49.1 %)	29 (17.0 %)	0 (0.0 %)

Source: own research.

Client influence occurred most frequently in the case of the valuation of large commercial premises and residential premises (apartments), and least frequently in the case of valuation of large residential properties (tenement houses).

7. Conclusions and final remarks

The property valuer is regarded as a profession of public trust. A valuer's role is to provide impartial opinions on value. The complexity of the valuation process and importance of valuation to the clients requiring the value of property have led to the regulation of the process through law and professional standards.

The conducted research confirms that partiality in property valuation is a feature of the valuation process. A significant source of partiality is the Valuer-Client relationship. A dominant influence on bias in valuation may come from various elements of both the client's and the property valuer's business environment, including non-compliance with the code of professional conduct. The issue of

ethics arises where the valuer is aware that the determined value could be different than if such relationship did not exist. Thus, the valuer faces a dilemma – comply with the rules of the impartiality of valuation or satisfy the client.

If non-compliance with the code of professional conduct may have a dominant influence on bias in valuation, an area requiring reinforcement becomes apparent. With increasing knowledge of the mechanism of the impact of the valuer-client relationship on value, the code of professional conduct should be reviewed, amended, propagated, and enforced³. Otherwise, public trust in the profession will be damaged. Such findings would be valuable for property valuers, valuation reports users - administrative bodies involved in land use policy, private investors, banks and scientists from economic, social and ethical disciplines.

It seems that the influence of the valuer on value is an area that has not been sufficiently researched.⁴ In Poland, the problem is exacerbated by toughening competition on the property market and decreasing valuation fees. Under these circumstances, a valuer is not a mere passive participant but is actually pro-active towards the client. The literature raised a pertinent question as to what professional organizations could do in order to make valuation more reliable. In the authors' opinion, it is essential to begin broad promotion (or even rewarding) of ethical conduct of property valuers and commence consistent enforcement of the code of professional conduct as soon as possible.

Last but not least, it must be noted that the authors are aware that the research methodology used in this article only allows general assessment of the nature, and especially the scale of the phenomenon of the valuer-client relationship and of the influence of this relationship on the property valuation process. The main cause lies in the researched matter itself – a phenomenon that is extremely complex and, at the same time, considered by many valuers private and embarrassing. As a result, it may prompt the respondents to give answers which are not always true.

8. Acknowledgements

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³ It is symptomatic in Poland that, out of numerous complaints filed with the Arbitration Committee, which is set up by a professional organization or with the Committee of Professional Responsibility, set up by the Ministry regulating the profession of property valuers, not a single one concerned non-compliance with the code of professional conduct. This may indicate poor awareness of the significance of the code to the valuation process.

⁴ This scanty research includes research conducted in Nigeria (IROHAM et al. 2012).

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