real estate

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Nation's Housing

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Panel: Appraisal Abuses Cost Taxpayers, Lenders

WASHINGTON — In a stinging criticism following a one-year investigation, a congressional subcommittee has concluded that ineptitude and fraud are rampant within the real-estate appraisal profession, and that taxpayers and lenders are losing billions of dollars as a result.

Inflated appraisals of homes and commercial properties have helped push hundreds of financial institutions into insolvency in recent years, the subcommittee said in a report released in Washington Wednesday. The impact of the national appraisal scandal is so pervasive, said congressional investigators, that only new federal regulation and industry self-policing can begin to correct the problems.

The House subcommittee on commerce and consumer and monetary affairs, which began its probe in 1985, found that:

- As much as 40 percent of the Veterans Administration's home-loan guaranty program's $420 million loss in 1985 was caused by dishonest or inaccurate appraisals. The faulty appraisals frequently overvalued homes, resulting in heavier debts for VA homebuyers, and bigger claims against the VA when borrowers were unable to make their monthly mortgage payments.
- At least 10 to 15 percent of the $1.3 billion in losses experienced by private mortgage insurers in 1984 and 1985 were directly attributable to faulty and fraudulent appraisals. One insurer who examined 300 defaulted home loans concluded that 40 percent of them involved defective appraisals.
- One of four of the 3,200 federally chartered savings and loan associations had significant appraisal problems in a 2½-year study that ended last October. The overvaluations by appraisers totaled a staggering $3 billion for those 800 savings and loans.
- Entire thrift institutions and banks have been destroyed by inflated appraisals. Two savings and loans examined in depth by subcommittee investigators — Sunrise Savings & Loan of Florida and Maryland's Community Savings & Loan — failed in large part because of real-estate appraisal abuses. The losses to taxpayers through the Federal Savings and Loan Insurance Corp. are more than $300 million at Sunrise alone.

The subcommittee placed the blame on three sets of shoulders, beginning with the appraisal industry itself. Of the 150,000 to 250,000 real-estate appraisers in the United States, the study found, barely one-third are affiliated with well-regarded professional trade organizations, such as the Society of Real Estate Appraisers or the American Institute of Real Estate Appraisers.

Most appraisers are "completely unregulated by anybody or any agency," said a subcommittee expert, Hal Lippman. In most states, anyone can hang out a sign and call himself an appraiser, without completing any formal training, examinations, licensing or regulation, Lippman said.

Large numbers of appraisers regularly and willingly succumb to "client-advocacy" appraising, the subcommittee charged. Such appraisers provide the lenders, borrowers or sellers who pay their fees "the numbers that make the deal work, rather than the true market value," said a staff member.

If a seller, buyer or lender needs a high home-value estimate to justify a particularly large loan, that's what he or she will get from a pliant advocacy appraiser. Or, if a client seeks an artificially low property value estimate — such as in calculating federal taxes owed on inherited real property — an advocacy appraiser will come up with the desired estimates.

Contributing significantly to the appraisal industry's problems, the subcommittee said, are lending institutions, federal banking and housing agencies, and quasi-federal home-mortgage intermediaries, such as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corp. (Freddie Mac).

Lenders in particular, the subcommittee found, often are more interested in collecting up-front fees from loan transactions than in the accuracy of the appraisals that underpin them. Federal banking agencies said investigators have inadequate appraisal-review standards and lax enforcement procedures.

What's needed for reform, said subcommittee chairman Rep. Doug Barnard Jr., D-Ga., is new federal legislation giving bank regulatory agencies authority to discipline appraisers who willingly or through gross negligence have misrepresented the value of real estate in connection with loans made by a federally insured lending institution.

Also needed are new national regulatory standards for appraisal quality, tougher oversight of lenders' appraisal records and new self-policing by the appraisal industry. In that regard, nine professional groups have agreed on a set of specific standards for all appraisals conducted by their members. The same groups are working to create a national appraisal-industry self-regulation board, modeled after one now used by the accounting profession.

A spokesman for the Chicago-based Society of Real Estate Appraisers declined to comment on the subcommittee's recommendations until officers study the panel's findings.