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Flipping, flopping and AMCs: Changes are taking place

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The appraisal process gets more and more interesting every day. Actually, the appraisal process stays the same; it's the environment in which the appraisal process takes place that is getting so interesting.

For years, appraisers were considered by many to have successfully completed their assignment if they came in at, or slightly above, the selling price. It's not true, but perception is reality - especially in real estate markets. During those years gone by, an appraiser had to watch out for property "flipping." That's the process in which buyers and sellers collude to inflate the selling price so that more money can be borrowed - and often the borrowed money would never be paid back. Now, appraisers need to be on the lookout for property "flopping." "Flopping" is the process where market participants collude to minimize a selling price. The objective here is to convince the mortgage holder to forgive a substantial portion of the outstanding loan balance, and make a "short-sale" work. In order for "flopping" to be successful, an appraiser's opinion has to match the opinion of the folks running the scam. Better yet, if the appraiser's opinion of value is lower than the sales price, it benefits the fraudsters even more. After all, these days people believe the appraiser has successfully completed the assignment if they value the property at or below the selling price. Sometimes a dishonest appraiser will actively participate in the fraudulent process, but more likely, it's an honest appraiser who just isn't sufficiently familiar with the market area. That happens because mortgage appraisal work is scarce, and people are accepting assignments further and further from their own back yards. They spend so much time - and gas money - travelling to the subject property that they have little time available to truly analyze the transaction.

Compound the "flopping" scams with the new roles of Appraisal Management Companies (AMC's). Regulatory agencies have insisted that the mortgage origination process be essentially shut off from the appraisal process. The objective is to prevent the person who might benefit from an improper value opinion - the mortgage originator or the government-insured lender - from having any influence over the person who provides that opinion, the appraiser. Consequently, the mortgage community has farmed out the responsibility for appraiser selection and review to a third party - the AMC. The thinking is that the "independence" of the AMC process will guarantee a reliable opinion. Trouble is the AMC is now on the hook (at least to some extent) for the value opinion. Naturally the AMC wants to limit its liability in the process. The easiest way to do that is to have a simple system of appraiser assignment. Typically, that system turns out to be an orderly rotation of assignments. If an appraiser is on the AMC's approved list, and there are nineteen other appraisers on that list, each appraiser will get every twentieth assignment - even if the assignment is fifty miles away. If appraisers reject the assignment because they feel they are not sufficiently familiar with a market area, they just go to the bottom of the list and wait until it's their turn again. The competent appraisers can afford to wait; the less competent appraisers can't.

So, the appraisers who know that they do not know a particular market are properly minimizing the opportunity for error, as well as their own risk. The appraisers who don't know that they don't know are getting the majority of the work - and maximizing the likelihood of error. The lender is off the hook because they delegated the appraiser selection process to an independent AMC.

The AMC is off the hook because it's not their opinion of value, and it's not their signature on the appraisal report, and it's not them that can lose their license to operate (they aren't licensed). And finally, the AMC is off the hook because they employed a system which randomly assigned an appraiser. The competent appraiser rejected the assignment, so he's off the hook. And the less competent appraiser who is desperate for any assignment ends up snookered by the fraudsters. So what happens to that appraiser, and what happens to the money?

Rest assured, at least for now, its government insured.

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