



Lessons from Litigation

Differences of opinion. Disagreements. Mediation. Lawsuits. Litigation. Even if you are vigilant in taking all of the necessary precautions to manage your risk of being sued, sometimes events and circumstances are aligned in such a way that a claim or lawsuit is unavoidable.

What are the current trends we are seeing in claims filed against appraisers? Overvaluation continues to be a frequent allegation, coupled with challenges to the selection of comps, or sometimes even overlooking a small attribute or condition that ends up having a negative impact on the ability to defend an appraisal.

Remember that whenever an appraisal is the subject of a claim or disciplinary action, it is scrutinized microscopically, and errors or omissions—even typographical errors that seem minor—can be magnified and harm the credibility of the entire work product.

Claims involving vacant land—or vacant land for development (as opposed to single lots)—can often be problematic and a frequent subject of litigation. Errors that are more black and white—failure to address a particular condition, such as a land use restriction, an easement, location within a flood plain, or sewer hookup—might be easier to defend, but are also frequent issues for claims made against appraisers.

Monday morning quarterbacking can be a useful exercise if we take a look at some recent claims and lawsuits filed against appraisers to determine what lessons can be learned and passed on to others. These are real situations gathered not only from Intercorp's Real Estate Appraiser E&O Program, but also from applications and requests for coverage we have received from appraisers who were insured in others programs and who may have been nonrenewed by their insurance carrier because of claim issues.

#1: Allegation--Overvaluation



In this example, we have a property that appraised for \$242,000. A retrospective review says it should have come in between \$215,000 and \$222,000. The difference is not enormous, not the hundreds of thousands of dollars that you see with some claims. However, the lender maintains that it *would not have made the loan in the first place* if the appraisal had not supported the value of the loan. Now in foreclosure, the claimant is seeking relief for considerably more than \$20,000 or \$25,000.

In a separate case involving overvaluation, the lawsuit specifically attacked the appraiser's "failure to analyze sales of comparable properties." Any time you get into a battle of the experts, there is generally room for differences of opinion, particularly in relation to selection of comps. In this case, however, the expert hired to review the appraiser's appraisal for the defense team had to conclude that the comp selection and analysis was indeed faulty, leading to an \$85,000 settlement.

Another claim for overvaluation (also alleging inaccurate and unsupported appraisals, failure to adequately inspect, etc.) comes from the Federal Deposit Insurance Corporation as receiver for one of the many banks that have failed in the past few years. When a claim for overvaluation is coupled with a charge that is more specific, such as failure to properly inspect, and this can be proven, it is much more difficult to defend.

A final claim example that alleged overvaluation turns into a nightmare to defend when the supervising appraiser thoughtlessly acknowledges in an email that she "did not know why the appraisal had come in so high unless it was a typo. . ."

Lessons Learned? Resist the temptation to fire off a quick response to an inquiry about one of your appraisals without reviewing and researching the file and seeking guidance from your E&O carrier or Pre-Claim Hotline for assistance. And, of course, document the reasoning behind your selection of comps, including why you decided not to use those that you deemed inappropriate for your subject.

#2: In over your head. . .



The allegations: Appraisals do not conform to USPAP; contain many errors which resulted in overvaluation. The appraiser, who was licensed to perform residential appraisals, misrepresented his credentials. Although the land was unzoned, it was clearly for commercial use which requires a certified general appraiser. Depositions in the case revealed the inexperience of the appraiser to handle this type of assignment, and this in turn, made it difficult to defend. (Case settled in excess of \$400,000.)

Lessons Learned: Stick to your areas of expertise; develop new areas of expertise after appropriate study, education, and guidance from a good mentor. Appraising vacant land has been and continues to be a "red flag" area for claims. If this is not within your area of proficiency, take a pass. (Note that some errors and omissions insurance policies exclude coverage for this type of appraisal, so check your policy exclusions as well.)

#3: Land Use Restriction/Failure to Identify Manufactured Home

In this particular case, the appraiser failed to disclose the existence of a land use restriction that severely reduced the value of the property, and also failed to use the proper appraisal form or to disclose that the structure was a manufactured home. There was also an addition constructed and added to the original manufactured home.

Lessons Learned: There are few excuses for lack of knowledge or poor preparation in understanding the common forms and requirements of the appraisal industry.

#4: Overlooking the Significance of a Few Little Words

“As is” and “as improved” – not many words, but their inclusion—or omission—in an appraisal can send a routine assignment on the road to court in short order. Here is an example: An appraiser appraises a 1200 acre parcel of undeveloped land for a developer, using the term “as is” to describe the property. Two years later, the appraiser is asked to update the appraisal “as developed,” which he does and labels the new appraisal as such, but without fully explaining the degree to which the development has been scheduled or occurred. The case was complicated further by poor documentation on the part of the appraiser when the new report was completed, making the appraiser’s defense even more difficult.

Lessons Learned: Choose your words and terminology carefully, and never assume that the reader of your report will automatically know what you think is obvious if it is not spelled out clearly. Further, meticulous documentation of what you do and why, your sources of information, and your reasons for including or excluding certain comps, for example, are invaluable in defending a lawsuit.

#5: Document, Document, Document



Following on the heels of the previous case cited is a more critical reminder of the need for thorough documentation. In this case a lender alleged overvaluation as well as violations of appraisal practice (no indication of sales/listing activity in the prior 12 months when the property had been listed) as well as the use of questionable comps.

With this lawsuit, however, the appraiser passed away before the claim could be settled; thus the file documentation will have to stand on its own as lawyers defend the lawsuit on behalf of the appraiser’s estate.

Lessons Learned: Can your appraisals stand on their own if you are not able/available to explain “what I really meant”?

#6: Square Footage – Do the math

This is a situation where a significant error in square footage (1800 square feet), coupled with an inaccurate drawing of a subject property, followed by the downturn in the market came together to create a \$100,000 claim for this appraiser. Without the market downturn, the impact of the square footage error might have been minimized, but the combination of circumstances is something like piling on in football or jumping on a bandwagon.

Lessons Learned: Never forget the common sense test. Do the numbers add up? Does my reasoning make sense? If this is the one house in the neighborhood that is 8,000 square feet when most of the rest are 6,000, is there a red flag? Is it really that much larger than the others? Is it time to double-check the data sources?

Elaine Matternas oversees Intercorp’s Real Estate Appraisers Errors & Omissions Insurance Program, now in its 18th year. ehm@intercorpinc.net