

Appraisers – a key element in real estate fraud prevention

While there are various types of fraud, this article is limited to frauds involving real property and financing.

One instance of fraud may be viewed as a misrepresentation of income, debts and the ability to repay a loan. If this type of fraud is looked at in the most positive of lights, it is the (possibly well intentioned) attempt by a borrower to obtain financing with the hope and expectation of making the payments to ensure the continuing ownership of the subject property.

A second type of fraud is the overinflation or misrepresentation of the value of the property in order to scam or deceive the lender into advancing funds for the benefit of the fraudster.

The obvious victim in both of these scenarios is the lender. From a lender's position, overvaluation of property causes an undervaluation of risk. This will affect loan loss reserves, profits and, if extended, may possibly affect liquidity levels.

If, because of fraud, a property is taken back by the lender and subsequently sold, because of inflation it may appear that there was no significant measurable loss. This is far from the case. When a financial institution is involved in a power of sale or mortgage foreclosure, the actual cost to the institution is often tens of thousands of dollars in legal fees, time and the employees' involvement in the procedure.

However, the lender is not the sole victim.



- Investors in the lending institution are also victims.
- Consumers are victims of fraud, when overstated property values are used by the various assessing departments to determine value in order to aid the municipalities in levying taxes.
- Appraisers are also victims because
 1. the 'bad apples' cause insurance claims, and
 2. the lending industry may start to negatively view all appraisers based upon the bad reputation of a few

The appraiser's signature is on the bottom line of the appraisal report, and, with our society's grow-

ing propensity to sue, the appraiser often ends up as the target of lenders who may have lost money. As fraud becomes more pervasive, appraisers are in the cross hairs.

The anecdotal information we have indicates the ironic reality that, without an appraiser and an inflated appraisal report, many frauds could not occur. This underlines the fact that the appraiser and his or her ethics are a key element in preventing real estate fraud. A further irony in this process is that, while the major participants in the fraud may share fraudulent profits in the range of hundreds of thousands of dollars, the appraiser's reward for his lapse of judgement is typically limited to

only \$300-\$500. For this, he or she has become a willing participant in the fraud, driven by the belief that cooperating in this scheme will deliver future business.

As the appraiser, it is not sufficient that you are aware and recognize any 'red flags' that may indicate a fraud situation. Additionally, you must be proactive in drawing these indicators to the attention of your client. The appraisers are the ones that the lenders rely upon to give them accurate, unbiased and professional opinions. In this regard, various members of the Appraisal Institute of Canada (AIC) officers have met with the financial institutions in order to determine their needs and how we can better serve them as clients.

This is only one level of communication and, in order to be truly effective and recognized as the professionals to be relied upon, the individual appraisers must also recognize their clients' needs and react to them.

For the most part, Canadians have a tendency to avoid being 'snitch cats,' however, if there is something suspicious or unusual about any transaction in which you are involved, you are being unprofessional by failing to advise your client. While we often hear anecdotal accounts about what has been observed by an appraiser, seldom does the appraiser actually call the AIC or formally refer the observation/situation for further investigation.

Just as it is your responsibility to protect and advise your client, it is also your responsibility to protect both your Institute and your fellow appraisers by reporting your concerns. Advising the AIC may be done in a confidential manner and would go a long way to ensuring the continuation of the high regard that the lending institutions currently have for members of the Institute. Remember, "If you are not part of the solution," you may very well be viewed as "part of the problem." 🐱

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