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## Compliance and Fraud

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### Appraisal Fraud & Abuse: Learning from the Last Mortgage Crisis to Address Today's Problems

By Thomas J. Inserra

The last mortgage crisis in the U.S. occurred from 1980 to 1995 and involved the failure of 2,912 federally insured financial institutions with combined assets of \$924 billion.

In an FDIC report prepared afterward, the agency noted that most of the assets of the failed financial institutions were "... secured by real estate mortgages and their disposition was hampered by a nationwide decline in real estate markets."

Congressional testimony and hearings concluded that fraud and abuses in the appraisal process were a contributing factor to the last crisis.

Among the worst losses at that time were incidents where lenders were found to have bribed, coerced or improperly influenced appraisers in property flipping scams where parties repeatedly sold property back and forth to artificially inflate its true value. These incidents demonstrated a breakdown in the appraisal process and compromised appraiser independence.

In a more recent 2007 survey, 90% of today's appraisers have reported that lenders have improperly attempted to influence the independent conclusions of appraisers. Although pressure exerted by loan officers and mortgage brokers was originally thought to have been an isolated issue, this national survey points to a potential industrywide problem, a more recent replay in the breakdown of the appraisal process and further compromise of appraiser independence.

To address the earlier crisis, a new corporation was formed in 1989, funded by the government and given the name of the Resolution Trust Corp. The mission of the RTC and its 8,614 employees recruited from the private sector was to recover as much money as possible for taxpayers, and resolve the crisis. The RTC managed 747 financial institutions with \$402.6 billion in assets. In comparison, Citicorp the largest U.S. bank had \$162 billion in assets at the time. Currently, Congress is now debating measures and attempting to determine if similar action will be necessary to solve this current mortgage emergency.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 created the RTC and established new mortgage lending policies. Armed with new legislation, federal regulators required all lenders, including those that sold mortgages on the secondary market, to observe new policies known as the Federal Interagency Appraisal Regulations.

These new regulations required that appraisals be prepared by an independent and unbiased licensed or certified appraiser. All 50 states were required to adopt new appraiser licensing laws and all appraisals were required to be prepared in accordance with the Uniform Standards of Professional Appraisal Practice.

In a recent 2007 investigation on appraisal practices, New York attorney general Andrew Cuomo discovered "... serious questions of conflicts of interest, negligence and errors [and] new policies safeguarding appraisal independence and bona-fide valuations must be established."

Look for more on this in future editions, which will summarize sweeping new appraiser independence policies affecting all lenders.

*Thomas J. Inserra currently serves as CEO of Zaiio Corp., an independent supplier of technology and appraisal services to more than 500 U.S. lenders. Mr. Inserra held prior roles as chief appraiser with Citicorp and national chief appraiser with Household Finance Corp. He served as national chief appraiser for both the RTC and FDIC during the last mortgage crisis, and has testified before Congress on banking and appraisal regulations. For more information, visit <http://www.zaiio.com>.*

