

"What Do I Do?" - Complaints And Claims Against Real Estate Appraisers

The target that seems to be on the back of real estate appraisers appears more real than imagined. Indeed, complaints and insurance claims against appraisers alleging an error or omission have steadily risen over the last few years, due in great part to turmoil in the real estate market. As property valuation is often at the center of many of the complaints and insurance claims, real estate appraisers have some justification in feeling that they are in "the line of fire". Predictably, there are many cases where the appraiser has committed an error or omission (for the purpose of this discussion we will leave out intentional acts of unprofessional or unethical behavior).

In many other cases, however, the appraiser may have committed no error, yet must still respond to the complaint or demand. This is where confusion often develops about if and how to respond and whether an appraiser should notify their errors and omissions insurance carrier.

Letters from regulatory bodies or attorneys cannot be ignored, yet appraisers may be hesitant to respond for a variety of reasons. Perhaps they feel there is no justification in the complaint and it will "go away". Maybe they are concerned about being sued and losing their license or their errors & omissions insurance, or at the very least seeing their premiums increase. While these concerns are real, a better understanding of real estate appraisers' errors & omissions insurance and what constitutes a possible claim and the obligation to report it can help an appraiser avoid confusion, or worse.

Errors and Omissions Insurance – An Overview

Most appraisers are covered under an errors & omissions policy, whether they have purchased it on their own or are covered under a firm's policy. E&O insurance can cover a broad range of actions or inactions relating to an appraiser's professional obligations and duties, and can be stated in a policy as "any act, error, omission (and in some policies Personal Injury) in the rendering of or failure to render Professional Services". A policy may go on to state that "the Company shall have the right and duty to defend any suit...even if the allegations of the suit are groundless, false or fraudulent" and that "the Company will pay on behalf of the Named Insured all sums which the Named Insured shall become legally obligated to pay as Damages for Claims". (It is important to note that insurance policies from different companies may offer different wording, coverage or features, including exclusions from coverage, and this information should be used as an example only).

Errors & Omissions policies also contain important information and definitions of what and who is considered an "Insured", what is a "Professional Act", what happens if the policy is terminated and so on. Many policies provide what are called Supplementary Payments for certain expenses or fees related to disciplinary proceedings or regulatory hearings.

Supplementary Payments provide payment or reimbursement for expenses in addition to or outside of a "Claim" and the limits of liability for the covered "Claim". Supplementary Payments can also include payments for loss of earnings if the insured needs to attend a hearing, or protection against discrimination or personal injury accusations.

The distinction of a "Claim" being covered under the policies liability limit, and "Supplementary Payments" being applicable for disciplinary or regulatory proceedings is an important one, as we will note below. An Errors & Omissions insurance policy defines and responds to a regulatory or board complaint or hearing differently than it does for a claim. This does not mean in any way, however, that an appraiser who is notified of a complaint by a regulatory body or official board does not have obligations under their Errors and Omissions insurance policy, or that their insurance might not be impacted.

Important Policy Definitions Every Insured Should Know

Most insurance policies include a major section called "Duties and Cooperation of the Named Insured" and may have sub sections entitled "Duties in the Event of an Act or Circumstance" and "Duties in the Event of a Claim". These sections can begin to help an appraiser understand how to respond should they receive notice of a complaint, hearing or claim. We can start with the definition of a "Claim". According to the policy offered by the Herbert H. Landy Insurance Agency through General Star Insurance Company, a Claim means "a demand for money, receipt of a request to provide a recorded statement, the filing of a Suit...claiming Damages and alleging an act, error or omission resulting from the rendering or failure to render Professional Services". It goes on to state that a Claim does not "include proceedings seeking injunctive or other non-pecuniary relief or administrative proceedings before any national, state, regional or local board".

So then, a complaint in front of a board is not a claim, and my errors and omissions insurance is there to cover claims, right? So I don't have to notify the insurance company if I receive a complaint letter because it's not a claim, right? Wrong!

Remember the "Duties in the Event of an Act or Circumstance" section? It states that if an Insured "becomes aware of any act or circumstance...that may reasonably be anticipated to give rise to a Claim, the Named Insured must notify the Company in writing as soon as practicable". According to Ted Gaisford, Vice President of Professional Claims at General Star Insurance Company, an "abundance of caution" should be used by any Insured receiving notice of a complaint or becoming aware of circumstances that could lead to such notification. Failure to notify an insurer could jeopardize coverage of the complaint or potential claim. Gaisford indicates there has been a marked increase in appraisers notifying insurers of complaints and hearings over the last couple of years. He further states that 75-80% of these complaints do not result in a formal claim, though payments from the insurer may still be paid under the "Supplementary Payments" section of a policy. With approximately 1 out of 4 complaints resulting in a formal claim, and supplementary payments often being made on the ones that are not formal claims, an appraiser must

recognize their obligation to the insurance policy as a legal contract (and this includes properly disclosing information on applications for errors and omissions insurance coverage).

Claims, Liability Limits and Supplementary Payments

When an appraiser purchases an Errors & Omissions insurance policy, one of the most important decisions is choosing the liability limits. Briefly, the liability limit is how much coverage is available should a "Claim" be brought against the insured appraiser. Liability limits are split, and may look like this: \$1,000,000/\$2,000,000. This means that the insured has \$1,000,000 per "Claim", with an "Aggregate" limit of \$2,000,000; the aggregate limit is the total amount of coverage available in a twelve month policy period should there be more than one "Claim" against the insured.

Note the emphasis on "Claims" and the way coverage is afforded for one, as we have already defined a "Claim" as not including "proceedings... before any national, state, regional or local board". This is where "Supplementary Payments" come in - to provide certain monetary payments or reimbursements outside of the liability limits. They can include payments for loss of earnings if an insured must attend a trial or hearing involving a "Claim against the Insured for Covered Damages". As noted previously, Supplementary Payments may be available if there is no "Claim", but the insured requires payment for attorney fees and other costs and expenses resulting from the investigation or defense of a proceeding before a licensing or real estate board or governmental regulatory body (note that commission disputes are typically excluded). Unlike the liability limits, there is usually no deductible to be paid by the insured if they receive Supplementary Payments under the policy.

What Do I Do Now?

Most policy holders would know what to do if they received a letter from an attorney, a client or another insurance company requesting damages or notification to collect damages because of an alleged error or omission on the part of the insured. Such notification would be an obvious indication of a "Claim" and the insured would be obligated to follow the notification and procedures as outlined in their policy and their insurance carrier.

What is less clear is what to do if an insured thinks there might be claim, or receives notice of a regulatory complaint. The policy states that the insured must notify the insurance company once they become aware of any "act or circumstance" that may "reasonably be anticipated" to give rise to a "Claim". As at least one out of four complaints results in a formal claim, it is clear that such a complaint can be reasonably anticipated to give rise to a claim, and an insured must report it. The reporting is also important for an insured to benefit from the Supplementary Payments available through the policy.

With all of this, there still may be some grey areas or confusion about what an appraiser should do to handle a situation. Appraisers insured with The Herbert H. Landy Agency through General Star Insurance Company have the benefit of a free and confidential legal hotline to consult with real estate lawyers familiar with claim, regulatory and policy issues for appraisers. Sometimes, the attorney might recommend a course of action that may help the appraiser avoid a claim or complaint and notifying the insurer, but if notification is suggested or required, the appraiser will have a much better understanding of the situation and be better able to work with the insurer's claim staff to resolve the problem. With some policies, an appraiser may have the right to choose their own attorney to address a regulatory or board complaint. Mr. Gaisford from General Star suggests letting the insurer choose the attorney, however. The insurance company's attorney may be much more experienced in resolving such matters, and can be instrumental in helping to avoid a civil complaint against an appraiser as well.

Recent Claim Trends

The majority of insurance claims against real estate appraisers are based on allegations of erroneous property valuations, and the huge increase in foreclosures has put property appraisals front and center. Many claims are still being filed over appraisals done three or four years ago when property values were at a peak. A common scenario is a home that was purchased with a mortgage made on the property and later the buyer defaults on the loan. The lender then goes back to the appraiser for damages, stating that the appraisal value was too high. A variation of this is the buyer, after buying at the top of the market, tries to sell after prices have softened and cannot regain their investment and sues the appraiser for the original "over valuation".

More recently, the valuation-related claims show a new characteristic: instead of claims being made for an over-valued appraisal, many current claims allege the property was undervalued. Appraisals done in the recent past during the current market are showing much lower valuations and claims are being made against these "low" value appraisals as homeowners have difficulty refinancing or obtaining equity loans. An even more recent concern is a "strategic foreclosure" – a property owner calculating the financial benefit of walking away from an underwater property, as opposed to using a short sale or traditional foreclosure. As strategic foreclosures become a calculated financial move for some property owners, the effects on claims against appraisers for valuations on those properties could be substantial.

Summary

An Errors & Omissions policy purchased by a real estate appraiser can provide significant piece of mind as the appraiser performs his or her professional duties, but that policy can also appear confusing, especially if an insured receives a legal notice or letter alleging an error. Understanding the definitions and features of the policy will provide an advantage to

any insured appraiser in responding properly to any complaint or claim and in working with their insurance carrier to maximize the protection afforded under the policy.

The terms, definitions and examples of insurance coverage are used here for demonstration only. Insurance policies and coverage can vary widely amongst insurance companies and you should consult an insurance professional and your policy for more information.

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The Herbert H. Landy Insurance Agency, founded in 1949, is a national leader in providing Errors & Omissions and Professional Liability Insurance to Real Estate Appraisers, Real Estate Agents and many other professionals.

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