Viewpoint: Broker Price Opinions Invite Abuse

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Though Congress continues to debate the need for financial reform and consumer financial protections, the widespread specter of valuation abuses, regulatory failure and mortgage fraud that inflated housing prices and directly contributed to the collapse of our nation's housing market is unabated.

In its current form, appraisal fraud is undermining the Obama administration's best efforts to turn around the economy, grossly deflating property values for working families and extending the "great recession."

Though many are familiar with the term "flipping" — an investor profits by acquiring real estate at a low price and quickly reselling it at a higher price or by buying a house that needs repair and fixing it up before reselling — today, the National Community Reinvestment Coalition, or NCRC, is increasingly hearing from homeowners and industry stakeholders who are being taken advantage of by companies seeking fast profits at their expense through "flopping."

Essentially, flopping works when a property's value is falsely deflated for a first purchase and then later resold at its true value. Flopping is a modern form of blockbusting, and it is destabilizing communities and the tax base throughout the nation.

The mortgage servicer or appraisal management company pays a real estate broker a nominal fee to determine the value at which the short-sale price should be set. The broker, succumbing to enormous pressure for a quick sale and a quick fee, sets its broker price opinion, or "BPO," at an artificially low price, well below the true market value. Then, often, the same or an affiliated broker in the same office will identify a new investor to buy the property, collecting a commission on the sale. Almost immediately, the investor gets an appraisal of the home and sells it at its true market value, pocketing the difference and perhaps kicking some back to the broker who initially set the low BPO.

Today, this abuse occurs when homeowners face a short sale of their home. Though organizations like NCRC work directly with homeowners and lenders to find sustainable mortgage solutions, sometimes keeping borrowers in their homes is impossible. In these situations, short sales are often the best option for homeowners, allowing them to gracefully relocate.

However, in using BPOs to determine short-sale prices, servicers, appraisal management companies and the real estate industry are leaving consumers, lenders and, notably, investors unprotected from and at serious risk of this new form of mortgage fraud. Flopping fosters a race to the bottom in real estate prices.

In the end, property flopping hurts everyone involved, except the broker: Lenders and investors are unfairly tricked out of a fair return on their investment; homeowners who might have been able to recoup some equity out of their home are unable to do so, and housing prices remain unstable and at risk of collapse. Meanwhile, brokers profit at each step along the way, and the tax base and the broader economy are negatively affected.

The only solution for protecting consumers, lenders and investors alike is to prohibit the use of broker price opinions in short sales and to return to using appraisals to independently determine a home's value.

Unlike BPOs, appraisals are done by trained professionals who have no financial interest in the property, in accordance with uniform standards of professional appraisal practice. BPOs, on the other hand, are determined by real estate agents and brokers, who inevitably have a direct interest in the property and who have inadequate valuation training.

Using BPOs is manifestly unfair to the lender and homeowner alike, and because BPOs are subject to almost no regulation to support independence and quality, using them easily leads to abuse and fraud. To make matters worse, brokers are competing on fee costs, driving appraisers out of business and leaving consumers with fewer options for an independent valuation.

To date no regulator has intervened on this issue, and no "watchdog" exists to stop an agent from giving a lowball BPO and then shepherding the property to a related party or a third party for profit. If we hope to restore investor confidence and dig out from the current financial crisis, we must end the culture of corruption that has permeated all levels of real estate finance, end the "gaming" of the well-intended Home Valuation Code of Conduct by appraisal management companies and follow the lead of more than 20 states in limiting the use of BPOs to realty listings and prohibiting their use in short sales.

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