The murky world of surveyors - Daniel Prince

What does the future hold for insurers?

"Do people think that if the current underwriting method and pricing remains that insurers will make money writing valuers over the next ten years?"

A quote from an RICS conference

"Valuers are pretty good at doing valuations but they are not very good at following the process"

This is not the only problem!

The role of the lender

- Main distributor of jobs and therefore key to the livelihood of valuers
  - Control fees paid
  - Control how many jobs
  - Control contract terms
  - Control their litigation approach
  - Control their audit approach
  - Control their own fraud prevention
  - Control their underwriting
  - Control the frequency of securitisation

- The majority of distribution contracts are through a tender process, run through procurement within the lender, are for a minimum of three years, involve an e-auction and are essentially focussed on the best price

- 10 years ago 50% of valuations were completed by in-house valuers, now 95% completed in the open market – they have actively shifted the liability from their own balance sheet and onto insurers via the valuers PI policy

The role of the panel manager

- Main winners of lender distribution contracts
- Often have in-house valuers and sub-distribute jobs to smaller firms
- Therefore key to the livelihood of smaller firms
- Characteristics:
  - Take 15-40% of lender fee for worked passed on
  - Can keep the best paying jobs or lowest risk jobs for themselves
  - Bid low knowing that when they have control of the work then valuers down the chain will have to accept the work
  - Control how many jobs go where and the quality of those jobs
  - Often promise to provide risk management and audit
  - Have strict SLAs with lender that may include substantial financial penalties

- Why did panel managers come about?
- Do panel managers provide value for money?

The role of the claimant solicitor

- At their best they want to correctly collect the money owed to lenders from the negligence of their valuers
- At their worst they hope by chucking enough mud that some will stick or that insurers will just want to cut a deal.
- The case of Webb Resolutions Ltd v JV Limited T/A Shepherd Chartered Surveyors – March 2013 provides an interesting quote which is below:

"What Rosling King did in this case was to produce an order that reflected the directions that they or their clients would like to have, and not the directions that the court in fact ordered. That is wholly unacceptable: it is not just unreasonable, it is verging on the contumelious. (adjective meaning scornful and insulting or insolent)"

- Limitation?
  - Facts - Contract = 6 years and Tort = 15 years
  - The big question - when does the clock start ticking....

The role of the economy / regulator

- Interest rates are key to repossession levels and in general every repossession leads to an attempted negligence claim
- Government change – can create changes in the supply and demand of housing which will drive changes in house prices
- Overseas investment – Super Prime London is seen as a safe place to invest for foreign investors but this could change quickly and the bubble would burst
- Help To Buy and other incentive schemes
- MMR – currently slowing the pace of the market but it does not cover the Buy To Let market and therefore new fringe / sub-prime lenders are popping up and people now applying for quasi BTL mortgages rather than going through MMR rules
- 10 lenders control 93% of the market and therefore the government is keen on new players but they will have to be more risk loving than the established players

The role of IT companies

- Only two players and one controls over 80% of the work being Quest giving them unbelievable power in the market
- Quest – built on 1987 technology. It has three main parts:
  - It is the way lenders and surveyors send info between each other
  - Q-Mobile – tablet device to collect info at the property
  - Q-Guard – fraud detection system

- Three AVM (Automated Valuation Model) providers
- Rightmove Plus and other data sources

What are surveyors up to?

- The larger firms are clearly improving their risk management controls and presenting insurers a better picture than before but the claims are still coming and this undermines the credibility of their controls. Are these claims historic or current and how long does it take to see the benefit of a change in risk management approach?
- Are controls robust enough to stop the surveyor who chooses to avoid them or thinks they slow them down?
- Those with Q-Mobile are often hand writing the notes and then transcribing onto the tablet in the car
- Lenders still want two page forms and request only those items that materially impacts value. If valuers see a blank box they feel they should put something in which can open them up to more problems when litigation starts
- Shortage of residential valuers
    - Average age is 55
    - Only 25 of 1200 graduates last year went into residential sector
    - Valuers moving from outside of their area
    - Firms trying to get non valuers to convert but no reward

What are surveyors up to?

- Have very short turnaround times (48 hours) imposed on them meaning little time to discuss or investigate plus the fee is often too low to allow this time
- Often do not know the LTV prior to accepting the job and therefore it is difficult to manage their own risk
- Lenders require unlimited liability
- Excess levels are increasing and therefore the small firms are under huge financial liabilities and many are unable to retire and/or trading insolvently
- They have no time to investigate lenders
- Have plenty of comparables but do they fully explain why the comparable is used, rejected or how adjusted? This is the key when a claim comes in.
- More automation of systems but not always with a positive outcome. A few examples seen in last few weeks from a major lender:
    - "There is an area of pubic open space to the rear of the property"
    - "We cannot guarantee that vacant passion will be given on completion"
    - "A main line rail station is located about 1 mile from these premises. Travel times to London (Waterloo) from this station on fast trains take about one hour."

There was no mainline railway station in this particular town and the nearest mainline railway station is 10 miles away. Apparently the paragraph above had been cut and pasted from another report

What are surveyors up to?

- Assoc RICS
  - Full RICS training takes five years (3 yrs technical / 2 yrs practical)
  - Assoc is finished in 18 months
  - No formal interview or review of work
  - No formal examination framework
  - All internally assessed
  - Must come from a property background

What are lenders up to?

- More reliance on AVMs and all remortgages may be done on this basis going forward
- Increased use of desktop valuations in conjunction with firms like Rightmove Analytics
- Due to limited resource they focus on high risk areas but fraudsters are now targeting areas where lenders use AVM and desktops. For example, find a high value property with a very low mortgage against it and request a further advance of say £150,000. For most lenders this would trigger no detailed checking and the monies are transferred before the real home owner makes the lender aware that the request did not come from them.
- Desperate for panel managers to deliver and offer them a risk management safety net
- Feel they pay fair fees
- Agree they are part of the problem and now keen to come to the table as running out of valuers and PI insurers
- Facing pressure about fees on mortgages
- Regulator is starting to look at valuation

Questions for underwriters to consider?

- Has the lender been considered?
  - Who are they? Where did they work before (e.g Mortgage Express are now UKAR)?
  - What is their approach to litigation?
  - What is their lending criteria / product range? – LTV, caps, BTL, HTB
  - What is their fraud response? (some lenders are currently getting 150/200 fraud alerts a day from Q Guard but only have the resource to check 50)
  - What parts of the country do they focus on?
  - What fees do they pay?
  - Do they use panel managers?
- What data sources are the firms using?
- How do they collect data and store it?
- What year did the valuation occur? What were economic conditions at that time?
- Do they limit liability?
- Is the firm just being passed high risk jobs by the panel manager?
- How easy are risk management controls to avoid?
- Is the firm equipped to value in a rapidly rising market?

Commercial valuation

- Greater complexity and bigger values
- Pressure on fees like residential – min fees dropped from £800 to £400 through competition for a reduced supply of work
- No central database of comparables
- Firms guard their comparables for a competitive advantage and have been known to feed false comparables to competitors
- Valuations are far more subjective as more analysis driven and valuer must consider that the same building can have different values based on tenant, length of lease etc
- Lack of systems
- Need to understand leases which often needs a legal mindset
- Deals are often highly leveraged and often quickly securitised meaning the original lender has very little skin in the game and the valuer is left exposed. Example of this is the Southern Cross case, 90% LTV, £1.5bn portfolio of 480 properties, valuer had 2 weeks to produce the report, securitised within 3 weeks. Valuers really need to understand the sector and clients they are working for to protect themselves.

General trends

The Pinnacle – remains unbuilt with little chance of completion
Untried developer using middle eastern money
Issue – was it ever the right type of development as banks need large floor area and not height

The Cheesegrater
Claim against project manager /steel manufacturer as precision cut steel was cut in China without supervision over quality control.
Large delays incurred as steel was cut incorrectly.
Should they have had a team in China. Highlights that we now work in a global supply chain.