

## **SDW Best Practices Discussion Paper**

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### **The Lender and the AMC Building a Successful Business Partnership**

The round-robin relationship between lenders and appraisal management companies is ages old. As far back as the mid 1980's lenders have been changing AMC's in mid-stream due to unsatisfying vendor relationships. This lack of satisfaction stems from a variety of problems all relating to quality, turn times, and general customer service. One AMC is contracted in place of another, and the pattern continues, as the subsequent management companies are unable to live up to customer expectations.

At a glance it would appear that this client/vendor relationship is relatively simple with regard to services to be performed. The AMC model should be able to bring the lender the solutions that the model promises: appraiser independence, ability to divest the fixed costs of employee appraisers, provision of quality control, appraiser recruiting and screening, appraisal products that conform to individual lender guidelines. However, the service level agreements and general understanding of client needs are frequently thwarted by lack of understanding and communication by both the lender and AMC.

#### **Dodging the Bullet**

Several years ago, when State Attorneys General came down on a few lenders for predatory lending and appraiser pressure, many flocked to the appraisal management companies to provide a solution. They needed a buffer between sales and the appraiser.

The AMC's, in their eagerness to pick up on this new found interest in their services, sometimes sent out sales people who were willing to promise service levels that operations would have a great amount of difficulty delivering. On the lender side, contract negotiators and vendor managers were eager to negotiate the best deal for the organization without a full understanding of the nuances and complications that arise daily in appraisal operations. While vendor managers had been experienced in negotiating pricing and turn times for automated products such as title, flood, and credit reports, the same black and white negotiations were not as precise a fit for appraisal services. But vendor managers pushed, AMC sales people responded, and the deals were made.

## **Understanding the Big Picture**

To add further complications, many of the vendors also supplied other settlement service products and were happy to bundle products and pricing to gain the best deal on the most profitable products. Deals have frequently been made on a corporate level and pressures have come to bear for some services to perform so that the more profitable ones would not lose business.

Examples and results of this type of negotiation have been seen in the recent past with large lenders and settlement service providers. However, everyone in the business is familiar with corporate pressures on operations to perform for the larger corporate benefit. Frequently appraisal services are negotiated as a “loss leader” to some extent, providing heavy discounting to obtain the business for other settlement services being offered. While this is an understandable business decision on a corporate scale, the individual business units are still expected to perform profitably for each of their individual bottom lines. While many of the services are strictly numbers driven, the lack of homogeneity within appraisal services makes it difficult to price without addressing exceptions that are not as unusual as one might expect.

The appraisal management organization provides its services through fee appraisers who must be dealt with on an individual basis. The properties being appraised are not always the “cookie cutter” property and include difficulties beginning with contacting the borrower, all the way through property, geographic, and market issues and complications. Any or all of these can easily affect the price demanded by the appraiser so that he may provide the expected product in a profitable manner.

## **Current Politics Increase both AMC Use and Pressures**

With the focus on appraiser independence issues and the failure of many lenders to provide that protective wall to obtain unbiased risk analysis, there are pressures on the lender to distance from the appraiser through use of outside appraisal services. Most lenders, not set up or even desirous of managing the necessary extensive appraiser fee panel, increasingly see the appraisal management companies as the solution to their problems.

As the slow market also increases lender competition, the relationship between the lender and appraisal management company becomes even more important. Often the appraiser “sinks the hook” with the borrower who is less likely to shop around for a loan if the process has already started with the appointment made for the property valuation and the inspection having already been completed. Client service requirements are more important than ever, as they can directly affect the lender’s ability to compete. A complete understanding of expectations from both the client and service provider is essential for the relationship to flourish in a partnership-like manner.

In order for everyone to be successful, there are basic business issues that need to be addressed during the formation of the service level agreement between the lender and the service provider. Without consideration of these issues, the business relationship is destined for frustration and ultimately failure. Most are uncomplicated and able to be addressed through understanding and flexibility from both parties involved. But they frequently become buried during the heat of

negotiation or are not addressed through corporate processes. As a result, the appraisal management company is set up to fail before they even begin to provide services.

The following are recommendations that will serve to point the way to success for both the lender and the appraisal management company.

### ***Recommendation #1 – Deal Negotiation***

- Does the lender’s vendor manager understand what the Chief Appraiser or underwriters need?
- Do both parties in the negotiation understand each other’s business requirements?
- Is the deal structured to provide ongoing relationship support?
- If the lender is using an RFP process, does the information requested really address the needs of the end user or is it more of a tool to design tight SLA numbers and advantageous pricing?

It is most important that the operations groups on both the lender and vendor sides are involved in the SLA discussions. Vendor managers are frequently too intent on negotiating the “best deal possible” for the organization – as that is their job. Sometimes the definition of the best deal is not what it may seem at the onset – cheaper and faster does not get the customer what they really want when it comes to appraisal services. Without appraisal operations being involved in the process, the vendor manager may end up negotiating a deal that is destined for failure, by simply not understanding that he is asking for the impossible.

On the vendor side, the sales person who is compensated by bringing in volume is likely to be willing to make agreements and worry about the performance later (or not at all). Performance is an operations issue, not a sales issue. The problems that arise from a poorly understood service level agreement can be avoided by involving someone in operations who knows the lay of the land with regard to existing workload, technology or operational workflow that may make it difficult or impossible to fulfill certain expectations the client may have.

In general, those parties directly responsible for supplying and receiving the appraisal products should be aware of the deal being negotiated and provide the insight necessary to design service level agreements that are satisfactory to the lender as well as obtainable by the vendor. There is no point in negotiating a good deal for the lender that is not designed to be achievable or beneficial to the lender and the vendor.

### ***Recommendation #2 – Jointly Agree on the Terms and Terminology***

#### **Turn times**

- From the time the lender orders the appraisal until it is received in hand?
- From the time of the appointment at the property to the time the value is communicated over the phone?
- Does the clock stop when the appraisal is first received by the lender or when it is finally acceptable?
- What happens when the appointment is difficult to make or the borrower is difficult to contact?

- What if the property turns out to be highly unusual or there are other delaying factors that are not discovered until the property inspection?

These are only a few of the questions that must be addressed and understood during SLA discussions. Vendor managers who are unfamiliar with the process may understandably consider appointment or borrower contact issues to be excuses. Some appraisal management companies may be successful in initially delivering the appraisal within turn time requirements every time. But if the quality of the appraisal or the lack of addressing lender requirements require the appraisal to be sent back one or more times for correction, the SLA turn time requirements may be satisfied but it certainly does not give the lender client what he is looking for in terms of service. More important than the specifics of the definition of turn time is that all parties feel that the requirements can reasonably be met.

### **Quality**

- Does the lender have expectations of also doing an extensive review of the report?
- Is the appraisal management company responsible for quality control of the appraisal before it is passed on to the lender?
- Are lender guidelines part of the definition of quality or is it specific only to the quality of the valuation number?
- Are appraiser qualifications part of the quality requirements or is it specific to the report itself?
- Are frequent requests by the lender for additional information or further explanation considered to be quality issues?
- Is the AMC quality check a clerical or technical review?

The answers to these and other related questions depend, to some extent, on the resources that the lender is willing and able to commit to reviewing the appraisal products as they are delivered. Specific expectations should be set at the beginning so that everyone understands what defines success and failure with regard to quality of the work being provided. Once the management company has a good understanding of the expectations, it can be controlled operationally through choice of appraisers, information supplied to that appraiser, and handling of the report once it is returned to the management company. Lack of understanding with regard to these requirements can frustrate the client who needs to put in much more time and effort than was originally expected. It can also serve to taint the reputation of the appraisal management company that is delivering what they thought was expected but is considered to be an inferior product by the end user.

### **Pricing**

There are a variety of hidden costs to the appraisal management company that are frequently not recognized. When the pricing to the AMC is driven down, there is little room to maneuver to address the less typical (but not necessarily infrequent) exceptional situation.

Pricing is one of the hardest hit issues in the negotiation between lender and appraisal vendor. A poorly executed pricing structure can be the death knell of an otherwise well designed SLA.

- Is the vendor provided any room to move on the fee to the lender if there are extenuating circumstances?
- How will it be addressed if the property is unusual or farther out geographically, resulting in an additional charge by the appraiser?
- How much time and money are allocated to the quality review process that the AMC is expected to provide?
- Does the lender representative understand the never specified but (unfortunate) reality of “you get what you pay for”?
- Is the lender requesting anything out of the ordinary with regard to guidelines or workflow that would increase time and costs for the AMC?
- Does the deal end up with “service creep” – the client continually asking for operational services or adding on appraisal guidelines and requirements without addressing these changes in the fees?
- Do lender requirements get buried in the AMC workflow so that the product received becomes more generic and less specific to what was initially agreed upon?

Ultimately, pricing needs to reflect the services being provided, and in turn, the vendor needs to make sure that if they are requiring premium pricing from the lender, that they are then providing premium service. It is up to the vendor to make sure that any additional services that have been promised to the lender are not lost in daily operational workflow. Exceptions to the norm should be reflected in the compensation to the vendor; however, the lender should then be able to always expect what has been promised.

Unusual guidelines provide information to the lender that is particular to their operational needs. However provision of exceptions whether it is additional information on the report, specifics as to communications back to the lender or with the borrower, or other needs that the vendor must accommodate, all can create hiccups in the vendor workflow. Not only does the vendor have to make certain that there are checks for these exceptions internally, there is also the communication to the appraiser that must be considered and is frequently where the fulfillment issues arise. Additional forms or other information that must be provided by the appraiser frequently requires follow up on the part of the AMC. While this is not the fault of the lender, both parties in the negotiation must recognize the issues around exception requests in the service agreement.

Fees negotiated by the lender and AMC should in some way reflect the appraisers’ pricing as well. While it would appear that lower negotiated fees are a “win” for the lender, the resulting products provided may be of a lesser quality than the client expects. If the AMC is not able to provide the appraiser with a competitive fee, the choice of appraisers may become limited or heavily weighted by less experienced appraisers.

Lower fees have also resulted in signature and inspection issues. Some appraisers may be willing to take on the work at a lower fee but cut corners by sending out a trainee to do the inspection and field work. The qualified appraiser signs the appraisal representing that he has done the work, but has made the process more profitable by not performing the work himself. This process is certainly not considered to be ethical, however it is practiced by some appraisers who point to the low fees being paid making it impossible for him to profitably provide the services without cutting corners in some way.

### ***Recommendation #3 – Ongoing Communication is ESSENTIAL***

The characteristics of a positive relationship between the AMC and their client lender all have a focus on communication. If time is invested in the business relationship up front it will pay off as things go forward and services are provided. Listed below are some suggestions that illustrate how communication at each step of the way is important and directly relate to all the issues discussed in the previous recommendations.

- Document the agreement as specifically as possible
- Have operations people participate in site visits to both the lender and vendor locations during the negotiations stage to better understand how each of the parties works and to begin to develop a face to face working relationship
- Document client guidelines and specifically discuss any that the vendor feels are not typical to ensure full understanding
- Vendor should develop a means to communicate all client guidelines to the field appraiser as well as to internal quality control groups
- Vendor should continue periodic lender site visits to address any operational changes that the client may have not communicated
- Participate in regularly scheduled operations conference calls that are initially held on a weekly basis and then spread out farther as the process runs smoothly
- Directly address any capacity planning issues to avoid dips in service
- Regularly review what is considered a “win” for both the lender and vendor to anticipate any changes in business requirements

### **Conclusion**

The working relationship between the lender and the AMC has historically been a rocky one. In retrospect, they have often started on an almost adversarial note, with contracts being won through stringent RFP processes and presentations that are highly competitive between the different AMCs and settlement service providers.

It is not a new business adage that communication is essential for good business dealings. It is particularly important when there are so many moving parts and so many parties involved that are not under the control of the lender and

vendor. A thorough understanding of client needs and vendor limitations is essential to design a successful service level agreement.

But it doesn't stop with the signing of the agreement. Needs and limitations change. Volume and loan programs change. Staffing and appraiser availability change. In a good partner relationship where each feels the support of the other, business requirements can be adjusted to fit the times. With today's changing markets, internal and external political pressures, and organizational upheaval a solid working relationship will go a long way to provide the top quality customer service that is essential to remain competitive. It is to everyone's benefit to work together to keep lenders and vendors in the in mortgage lending strong and successful.