# Valuers' Liability in Mortgage Valuation

**Gabriel K. Babawale**

*University of Lagos, Nigeria*

## INTRODUCTION

In developed countries, claims against valuers for professional negligence have increased over the years (Brownell, 2000). Murdoch (2001) proffered two reasons for the increase. One, clients are now more aware of their rights; two, increased media coverage has alerted the public to making large claims for professional negligence. Murdock (2002) observed that:

*"…fifty years ago, the vast majority of reported actions brought against property professionals arose out of residential building surveys. Today, the picture is very different; residential and mortgage valuations, once regarded by general practitioners as a safe, albeit modest sources of income have become a very thorny thicket as both lender clients and house purchasers have been quick to pounce on any error in the report and turn on the surveyor. Even more worrying, in terms of the sizes of claims and their potential impact on professional indemnity insurance premium, has been the growth in claims by financial institutions which, having lent on the security of commercial property when times were good, learn to their cost that markets fall as well as rise, and seek to lay off their losses on their professional advisers (especially valuers) when their property company borrowers default".*

Babawale (2007) supported this view when he remarked that, with globalization and increasingly complex economic landscape, the 'immunity' long enjoyed by Nigerian valuers to litigation for negligent valuations would soon cease.

The objectives of this study are to: show: (a) what duty of care the valuer, being a professional, owe his clients in law with particular reference to mortgage valuation; (b) show the aspect of the mortgage valuation process where valuers are most vulnerable to negligence; (c) define the limits of the duty of care that a valuer owes in mortgage valuations by reference to relevant practice standards and case laws;

(d) and offer pragmatic steps to minimizing exposure to liability for negligence in mortgage valuation. The results are expected to be of great benefit to all stakeholders - valuation profession, lending institutions, borrowers, judicial officers, insurers, and particularly valuers. In the emerging globalized world, valuations that would be relied upon internationally can be produced only by a valuation profession that conforms to international standards of professional education, competence and practice.

The study has Nigerian valuers particularly in mind. The ultimate aim is to help Nigerian valuers hone their skill in mortgage valuation generally; and specifically to serves as a wakeup call to erring and unwary valuers; and provide practical steps to avoid potential liability in mortgage valuations. Though reported cases of professional negligence involving real estate valuers in Nigeria are increasing by the day; such complaints have hardly gone beyond the disciplinary committee level of the regulatory bodies: the Nigeria Institution of Estate Surveyors and Valuers (NIESV) and/or the Estate Surveyors and Valuers Registration Board of Nigeria (ESVARBON). There are therefore scanty or no known records of court adjudication on negligence cases involving property valuation, particularly for mortgage purposes. For this reason, the paper focuses on court pronouncements in countries of common jurisprudence as Nigeria.

The study is in three main sections. The next section considers court pronouncements that tend to define and qualify valuer's duty of care with particular reference to mortgage valuation. The last section concludes the study and includes strategies that could help valuers prevent, or at least, minimize liability in mortgage valuation.

## REVIEW OF LITERATURE

Property valuation is the art and science of determining the monetary value or worth of an interest or right in property encompassed in an ownership for a particular purpose, and at some specific date. The peculiar characteristic of the property market makes the services of real estate valuers imperative. Unlike the market for equities where investment asset prices can be quickly and easily imputed from prices of identical assets that are publicly traded in active secondary markets, real estate transactions occur relatively infrequently, the products are heterogeneous; the market is highly fragmented, and the quality and quantity of market information is poor. In spite of this, information on the market value of real property investments is often required to support financing and investment decisions such as sales and acquisitions, current cost accounting, insurance policies, securitizations, the measurement of historic investment performance and analysis of credit and collateral, without necessarily having to take the property to the market for sale. It is in this regard that valuation comes in as proxy for actual transaction prices or as surrogate for prices of sold property (Bowles, McAllister & Terbert, 2001). The whole basis of professional property advice therefore rests on the assumption that valuations are good proxies for prices (Waldy, 1997). This belief or assumption speaks of the pivotal role that valuation is expected to play in the overall workings of the property market. The International Valuation Standard Committee (IVSC) once remarked that real property represents a considerable portion of the world’s wealth, and its valuation is fundamental to the viability of global property and financial markets (IVSC, 2003).

History is replete with adverse repercussions of inaccurate valuations on the property and financial markets and by extension, on the whole economy of nations, regions and the entire world. Beside the potential grave repercussion on the economy, inaccurate valuation is detrimental to the credibility and relevance of the valuation profession. According to Brown (1991), if valuations have only a limited likelihood of accuracy, clients may question why valuation is necessary at all and it could mean that performance measurement for investment properties would be a fruitless exercise. The apparent lack of coherent and consistent results from the valuation process has damaged the reputation of the valuation profession (Bretten & Wyatts, 2002). More particularly, inaccurate valuation exposes the valuer to liability for professional negligence.

The courts have always looked up to the published standards of professional bodies for judgment guidelines. The case of Craneheath Securities v York Montague (1994 and1996) (Court of Appeal) emphasizes the importance of attention to institutional guidance. While failure to comply with these standards do not in themselves constitute a breach of the laws as they are not legislative enactments, the courts have always put these standards into consideration especially in liability cases such as negligence, breach of contract, and fraud (Shampton, Waller & Waller, 1998). Hence, the grounds for valuers’ liability for negligence would be uncovered by examining the relevant case laws and court pronouncements, and also by looking into the practice standards and guidance prescribed by relevant professional bodies.

In Nigeria, the real estate valuation profession is jointly regulated by the Nigerian Institution of Estate Surveyors and Valuers (NIESV) and Estate Surveyors and Valuers Registration Board of Nigeria (ESVARBON), the former more prominent. Such regulations include setting minimum standard for registration as licensed or certified valuers and prescribing mandatory practice standards and ethics. Besides its own provisions on practice standards, the latest Valuation Standards and Guidance Notes of the Nigerian Institution of Estate Surveyors and Valuers (2006), mandated valuers to comply strictly with the ethics and standards stipulated by the International Valuation Standards Committee (IVSC), in their valuation construction and reporting. Specifically, section 8.2.4.1 provides that in performing valuations of property where the result will be used to obtain loans, mortgages and debentures, valuers shall normally estimate the market value of such assets in accordance with the International Valuation Standards.

## *THE NATURE OF MORTGAGE TRANSACTION*

A mortgage is a transaction whereby a lender (the mortgagee) accepts a claim or title for property from a borrower (the mortgagor) as security for the payment of a loan for which the property is given. It is a pledge of an interest in property as security or collateral for repayment of a loan with provision for redemption on payment (IVSC, 2007).

If the mortgagor defaults in his obligations, the mortgagee has a number of options opened to him to recover his loan. He may sue the borrower on the personal covenant; take possession and sell the property and apply the proceeds to repay the loan and any arrears of interest; or may apply to the court for a foreclosure order which will have the effect of extinguishing the mortgagor's equity of redemption. The mortgagee may also at any time take possession of the income from the property, and after paying all necessary outgoings may apply the balance to paying interest on the mortgage debt, including any arrears as well as apply any surplus to reduce the mortgage debt. Alternatively, the mortgagee may appoint a receiver to collect the income from the property and apply it to the purposes of discharging the loan.

It follows from the foregoing that the mortgagee's remedies are only fully available where the market value of the property exceeds the amount due to the mortgagee, and the net income from the property is sufficient to cover the annual interest on the loan with a margin to cover possible arrears.

## *THE MORTGAGE VALUATION PROCESS*

A mortgage valuation is the estimation of the value of a property to be used as collateral for a loan (Ajayi, 2009). Mortgage valuation is required in loan underwriting process to determine the degree by which the value of an asset exceeds the loan in providing the margin of asset cover or the loan-to-value ratio. It is also an integral part of capital adequacy systems which attempts to manage the risks taken by lenders. Valuation therefore plays an important role in the bank lending process. To play this role creditably, valuations must provide a good proxy for actual transaction prices otherwise decision, including analysis of credit and collateral would be taken on false premises with potentially grave consequences.

Where the loan granted on the basis of a mortgage valuation is duly repaid, no issue on the mortgage valuation would arise. However, where the loan is not repaid and the mortgagee exercises the right of foreclosure, the valuer's report relied upon for the loan advance is put to test. If the amount realized at the foreclosure sale covers the loan advanced, the valuation report would have passed the test. However, if the mortgagee could not recover the amount stipulated in the valuation report, the report is called to question and the valuer may be liable for professional negligence.

In making a valuation for mortgage purpose, the ordinary principles of valuation apply except that the valuer is expected to pay specific attention to the mortgagee's position in relation to the property and to the remedies available to him in the event of default by the mortgagor. The basis of mortgage valuation is usually the market value (MV), as the lender is primarily concerned with how much the security would sell in the open market in the event of default by the borrower (Ajayi, 2009). Market Value is described as:

" *…the estimated amount (price) for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion*" (IVSC, 2011).

Both the valuers' training and valuation regulatory bodies generally prescribe a systematic step-by-step process the valuer is mandated to follow through from valuation instruction to arriving at opinion of value. The valuation process is a systematic, logical method of collecting, analyzing, and processing data into intelligent, well reasoned value estimates (IVSC, 2011). The International Valuation Standards Committee (IVSC) prescribed an eight-step valuation process model comprising the definition of problem (identifying the legal, physical, and economic characteristics of the property including the scope of the assignment and limiting conditions); site inspection and market studies; data collection, selection and analysis; choice of appropriate valuation basis and method(s); reconciliation of values indicated and arriving at the final opinion of value; and reporting of the defined value.

Wyatt (2003) noted that inaccuracy (and other errors that provide grounds for negligence) can be introduced into the valuation process at any stage beginning from the instruction given by the client through to inspection of the property, selection of comparables, valuers' approach to the valuation, choice of method (s), calculations to arrive at the defined value, and the final valuation opinion, which may be adjudged accurate or inaccurate.

## *NEGLIGENCE IN MORTGAGE VALUATION*

The issue of negligence is a matter of law. Negligence is founded on the basis of the existence of a duty to exercise care or professional competence in performing a particular task. Merely assuming a professional title is enough to alert the public to the fact that the individual may be relied upon to exercise a professional standard of care. Failure to exercise the skills necessary to protect the client's interest will constitute a breach of duty. In strict legal analysis, negligence means more than heedless or careless conduct, whether in omission or commission; it properly connotes the complex concept of duty, breach and damage thereby suffered by the person to whom the duty is owed (Lord Wright, undated).

## *THE NATURE OF VALUERS' DUTY OF CARE*

The first question to be determined in any action for negligence against a valuer is whether the valuer owed the plaintiff a duty of care. Kodilinye and Aluko (2001) claimed that in general, a duty of care will be owed wherever in the circumstances it is foreseeable that if the defendant does not exercise due care, the plaintiff will be harmed. This foreseeability test was established by Lord Atkin in Donoghue v Stevenson (1932) in what is known as "the neighbor principle". The principle states that you must not injure your neighbor who the court described as:

*"persons who are so closely and directly affected by my acts that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions which are called in question"*.

Also, in R v. Cognas Inc; the Canadian Supreme Court ruled, inter alia, that for negligence to succeed, the plaintiff must prove that the valuer owed him a duty of care; that the said representations were untrue, inaccurate or misleading; that the valuer acted negligently in his representations; that it was reasonable for the plaintiff to rely on the valuer's representations; and that the plaintiff incurred loss(es), suffered injury or detriment as a result of relying on the presentations of the valuer. Thus, in Platform Funding v Anderson Associates, a UK court acquitted an evidently negligent valuer because the court found that the valuation would still have been the same even if the valuer had done his work well**.** The court found that the losses suffered were largely caused by the seller's fraudulent scheme.

### *VALUERS' DUTY OF CARE MAY EXTEND TO A THIRD PARTY*

Usually, a substantial majority of instructions to valuers come from a lender which naturally establishes contractual relationship between the lender and the valuer. The question invariably arises whether any legal liability is created between the valuer and the prospective borrower. The principle of privity of contract ensures that only parties to the contract can sue a valuer for breach of contract for loss or injury suffered as a result of the valuer's action. Thus, in the early case of Davis v Sprott (1960), the position was that no such liability exists, as the contract is with the lender; no duty is owed to the borrower. However, the valuer's action in tort for negligence often extend to certain persons who are not the valuer's direct clients but whose relationship with the valuer is adequately proximate one as established. That is, a valuer's liability for negligence may extend to a third party as the court requires the valuer to foresee a third party beneficiary (i.e. other than the valuer's client). This is particularly true of valuations prepared for mortgage institutions where the court often presumes that the purchaser is owed a duty of care by a valuer instructed by a lending institution to carry out a mortgage valuation of the property to be purchased. Thus, in Graham v Pimr, Garm [1985], the court ruled that "an appraiser owes a duty of care not only to the client on whose instructions he carries his appraisal but to all other persons to whom it may be shown and who might be expected to rely on it in dealing with the subject matter by way of purchase, mortgage, security or otherwise".

Likewise, in Smith v. Eric Bush (1988), it was held that a firm of valuers which had carried out a mortgage valuation on a piece of property, on the strength of which a purchaser suffered loss, is liable for negligence. The judge was of the view that the valuer assumes responsibility to both mortgagee and purchasers by agreeing to carry out a valuation for mortgage purpose knowing that the valuation fee has been paid by the purchaser and knowing that the valuation will probably be relied on to decide whether to enter into a contract to purchase the house or not. In Corisand Investment v Druce and Co. (1978) where the borrower initiates valuation for mortgage purpose and the valuer for various reasons negligently performed the task, the court held that the valuer owes the lending institution duty of care even though he was instructed by the borrower. The principles were further consolidated in Australian cases of Mutual Life and Citizens Assurance Co. Ltd v. Evatt; and Shaddock & Associates Pty v. Parramatta City Council.

### 3.3. *VALUER'S DUTY OF CARE IS NOT UNLIMITED*

It is stating the obvious to say that not all third parties are in a position to sue a negligent valuer. To avoid the problem that the American Supreme Court Justice, Benjamin Cardozo, once referred to as "liability in an indeterminate amount for an indeterminate time to an indeterminate class", the court has tried to sift the third parties that valuers reasonably owe a duty of care. In Hercules Management Ltd. v. Ernest Yong, the Supreme Court of Canada proffered two guiding tests for delimiting the categories of people who are covered by the valuer's duty of care: the limited class test, and the forseeability test. In the former, the claimant needs to show that s/he belongs to a class of people whose use of the work is known by the valuer; while in the latter, the claimant need to show that the valuer could reasonably have foreseen the use of the work by a class to which he (the claimant) belongs.

### *THE IMPLICATIONS OF DISCLAIMER AND LIMITING CONDITIONS*

Valuers often insert in their valuation reports disclaimer and limiting conditions intended to exonerate the valuers from obligations to any third party beside the client that commissioned the valuation. The implications and effectiveness of such clauses in exonerating valuer from liability is unsettled. Canadian courts generally recognize such clauses as valid as demonstrated in Wolverine Tube (Canada) Inc. v. Noranda Metal Industries Ltd where the disclaimer was in the form:

*"Any use which a third party makes of this report, or any reliance on or decisions to be made based on it, are the responsibility of such third parties…..accepts no responsibility for damages, if any, suffered by any third party as a result of decisions made or actions based on this report."*

The court accepted this clause as valid in warding off a third party who used the report and later sued the valuer for negligence.

Also in Royal Bank of Canada v. Burgoyne, the disclaimer and limiting conditions reads thus:

*"The distribution of values in this report, between land and improvements, apply only under the program of utilization as identified in this appraisal. The separate evaluation, as estimated herein, must not be used in conjunction with any other appraisals, and may be invalid if so used. The client to whom this report is addressed may use it in deliberations affecting the subject property only, and in so doing, this report should not be extracted, but used in its entirety. (...) In preparing the foregoing Appraisal Report, the undersigned appraiser has employed the usual methods and procedures used by Appraisers in Nova Scotia, and the result is the product of his careful and considered opinion. However this Appraisal Report is the opinion of the appraiser only - and under no circumstances whatsoever shall the Appraiser personally, be held liable for any loss or damage that may occur to any person or persons by reason of their reliance upon this Appraisal".*

The court also upheld this disclaimer, limiting condition/assumption in restraining the bank, a third party, from succeeding in the action against the negligent valuers.

However, in Rumack v. Amstrong, the court refused to allow a disclaimer which excluded third parties from use of a valuation report to save a negligent valuer who knew quite well that his client would use the report to seek for credit facility even though the time and the particular financier were not known as at the time of the report.

***PENALTY FOR NEGLIGENCE***

Ordinarily, the valuer should bear the full loss suffered by the claimant in negligence cases. If for instance, a property is valued for N100 million, but ends up actually being sold for N80million, the N20 million difference would ordinarily be awarded as damages against the valuer. However, where contributory negligence on the part of the client/claimant can be inferred or proved, it can successfully be pleaded to ensure that the valuer makes good only the proportion of the loss caused by his own proven negligence. In Australia, proportionate liability is not just rooted in common law but is now statutorily provided in the *Civil Liabilities Act* 2003 (Qld). Thus, in the Australian case of Kayteal v. Dignan (2011) NSWSC, the valuer negligently valued a mortgaged property for $1.2million when in fact the value should be $52,000. In packaging the mortgage, the solicitor noticed discrepancies in the valuation report and the subject property and drew the valuer's attention to it but the valuer confirmed the report. The solicitor however did not communicate his observation and the valuer's response to the client lender. The court found both the valuer and the solicitor guilty of professional negligence; the solicitor, because he did not communicate the valuation discrepancies to the client.

The court equally found the borrower/client as contributor to the lender's loss as he knew quite well that the valuation of $1.2million was faulty having bought the same property two months earlier and must have misrepresented the purchase price to the valuer. The court consequently awarded 47.5% of the damages against the borrower, while the valuer and the solicitor were made to bear 40% and 12.5%, respectively – proportionate liability.

The position of the courts with regard to losses suffered as a result of economic down-turns which the valuer could not reasonably have envisaged is inconclusive. In the UK case of *South Australia Asset Management Corporation v. York Montague Ltd (1996) –popularly referred to as BBL or SAAMCO case* - the House of Lords sought to limit the liability of the valuer by ruling the valuer was only responsible for the loss suffered as a result of the valuation being wrong but not for the entire loss suffered by the financier as a result of a downturn in the property market. This position was justified on the ground that the loss suffered as a result of a downturn in the property market is a risk that the financier ordinarily bears as part of his normal business of lending money for property transactions.

However, the Australia Appeal Court in Kenny & Good Pty Ltd v MGIGA (1996), in a similar circumstance, ruled otherwise that the valuer is liable. In this case, the valuer carried out a valuation for mortgage purpose of residential property which was nearing completion. The valuer presented a figure of $5.5m on the property "as completed" with assurance that the property would remain good security for loan of 65% of the valuation up to a period of five years, showing an exceptional knowledge of the market. The valuation report was relied on to advance a mortgage at 65% of the valuation figure and to issue a mortgage indemnity guarantee policy. The borrower defaulted at a time when there was a sharp decline in the property market; leaving the lender and the insurer with considerable shortfall. It was discovered that the property at the date of the defendant's valuation was between $3.9m and $4m. It was held that the whole of the lenders loss was caused by the valuers' negligence and was not too remote. The valuer was held liable for the full extent of loss of the financier and mortgage insurer including the loss that resulted from the downturn in the property market. According to the court, the financier would not have entered into the transaction but for the valuer's negligent advice.

However, where it can be proved that the client/lender would still have suffered the loss suffered even if the valuer had correctly predicted the value at which the property was subsequently sold (e.g. $5.5m in Kenny & Good Pty Ltd v MGICA), the valuer would not be liable. "A person who negligently provides information or advice should not be held liable for loss that would have been suffered if the information or advice were correct".

The decisions in South Australia Asset Management Corporation v York Montague Ltd *[1996]* seem to provide some universal yardsticks for determining the extent of a valuer's liability for negligence as follows:

• If an accurate (i.e. non-negligent) valuation would have prevented the lender from advancing the loan, the valuer is potentially liable for all of the lender's losses resulting from the loan.

• If an accurate valuation would have resulted in a smaller loan being made, the valuer is potentially liable for the difference between what has been lent and lost and what would otherwise have been lent and lost.

• In either case the valuer's liability is subject to a "cap", equivalent to the amount by which the property has been over-valued. Accordingly valuers can never be held responsible for more than the amount of their error.

That is, the principles involve estimating how much loss the lender suffered and how much loss (if any) would it have suffered if there had been no negligence. The valuer's liability is the difference between the two.

***ASPECTS OF THE MORTGAGE VALUATION PROCESS WHERE VALUERS ARE MOST SUSCEPTIBLE TO NEGLIGENCE.***

***PROPERTY INSPECTION AND MARKET/INDUSTRY STUDIES AND ANALYSIS***

For secured lending, the practice standards of the Nigerian Estate Surveyors and Valuers and the International Valuation Standards provide, among others, that valuation reports shall make reference to the approach or approaches adopted, the key inputs used and the principal reasons for the conclusions reached. It is further provided that valuation reports should include comment on factors that are relevant to a lenders assessment of the performance of security over the life of the proposed loan. Such relevant factors include the current activity and trends in the relevant market; historic, current and anticipated future demand for the type of property and location; any potential, and likely demand for, alternative uses that exist or can be anticipated at the valuation date; and the impact of any events foreseeable at the valuation date on the probable future value of the security during the loan period. In addition, it is mandatory that the investigations made during the course of a valuation assignment be adequate having regard to the purpose for which the valuation is required and the basis of value to be reported; that sufficient evidence shall be assembled by means such as inspection, inquiry, computation and analysis to ensure that the valuation is properly supported.

The valuer therefore owes it as a duty to the client to spend "reasonable time" in gathering relevant and sufficient data; and carry out thorough data analysis that would enable him come up with reliable value opinion in all circumstances. In Perry v Sidney Phillips and Son [1982], the valuer made a series of mistakes on the ground that he "at the time was under considerable work pressure". While holding the valuer liable for negligence, the judge refused to consider lack of time as an argument for the valuer's defense. In New Zealand Valuers Board of Appeal v Donald Davis Ferguson, the valuer knew he needed up to two weeks to prepare and compile the valuation report. The purchaser however demanded that the report be ready the following day, failing which the instruction would be withdrawn. The valuer hurriedly prepared the valuation to make it available the next day as requested. As a result, the valuation figure went up from NZ$8.8 million to NZ$10.5 million. The Board of Appeal found the valuer guilty for acting unprofessionally by accepting to do the valuation in a hurry, thereby failing to do certain things he should have done.

In the Canadian case of Aura Financial Services Canada Ltd v. Jakubiec, the valuer based his valuation solely on the property owner's opinion of the property's resale price without substantiating with recent sales comparables or cross-checking with local property agents in the manner of a prudent valuer. The court therefore found the valuer liable for negligence for failure to acquaint himself with the subject property, its surroundings, and the general state of the neighborhood, and for not adequately carrying out the required market survey and data analysis. Also in Kakanee Mortgage MIC Ltd v. Concord Appraisals Ltd., another Canadian case, the valuer was found liable for failing to adequately inform himself and verify the reliability of the comparables he relied on to assess the property value. The valuer was also found guilty of double-counting, several glaring errors and omissions, and failing to identify a "no build" restrictive covenant (Chartered Business Valuators, 2010). In Indian Head Credit Union Ltd v. Hosie A. (1994), the valuer was found guilty of negligence because he spent only 50 minutes to inspect a building with manifest structural defects that affected the value negatively, and also failed to make further enquiries from neighbors and to obtain Engineer's report on the structure.

However, in Mount Banking Corporation Ltd v Brain Cooper (1992), the valuer escaped liability largely because the valuation file demonstrated good preparation, including various permutations of the figures, and because all relevant matters had been considered in arriving at the valuation (Bretten and Wyatt, 2002). Also in

Craneheath Securities v York Montague (1994 and 1996), the valuer's use of the RICS Valuation Guidance Notes in reporting to the lender was instrumental in enabling him escape liability (Foster et al., 1997).

### 3.6.2 *FAILURE TO DISCLOSE MATERIAL INFORMATION*

Section 9.10 of the Valuation Standards and Guidance Notes of the Nigerian Institution of Estate Surveyors and Valuers provides that the valuation report should disclose any assumptions, hypothetical scenarios, or limiting conditions that may affect objectivity and that directly affect the valuations and, where appropriate, indicating their effect on the value. This provision, among others, makes the valuer liable for failing to disclose material information. In Finance America Reality Ltd v Blade, Prassin, the Supreme Court of Nova Scotia found a valuer negligent for failing to disclose to the lender that approval for a sub-division upon which his valuation was predicated hasnot yet been obtained. Similarly, in a Malaysian case, Bank Bumiputra Malaysia v Yeoh Ho Huat [1971], where a developed site was valued by the defendant, a certified appraiser at M$40, 768 as security for a loan of M$20, 000. The land was found to be swampy, much of it under water, which could only be sold for M$7, 600. The court held the valuer liable for the loss suffered by the bank for not disclosing the true position of the land which if the bank had known the loan would not have been advanced.

### 3.6.3 CARRYING *OUT VALUATION OUTSIDE AREA OF COMPETENCE OR IN UNFAMILIAR MARKETS*

According to the International Valuation Standards "because valuation requires the exercise of skill and judgment, it is a fundamental expectation that valuations are prepared by an individual or firm having the appropriate technical skill, experience and knowledge of the subject of the valuation, the market in which it trades and the purpose of the valuation". It is of paramount importance therefore that the valuer should have sufficient knowledge of the market in which he operates and the skills necessary to undertake a particular valuation. More specifically, the Royal Institution of Chartered Surveyors (RICS) Practice Statement 1.5 (1) provides that where the valuer does not have the required level of experience to deal with some aspects of the commissioned property then s/he should seek assistance from specialist valuer, environmental surveyors, and other relevant professionals (RICS, 2010). Crosby et al.(1998a) made reference to William Raymond Wright (where a valuer trained in rural valuation and who has had several years of practice in his home area where he specialized in farm business "suddenly emerged two or three years ago and commenced valuing a range of urban and rural properties all over New Zealand". The Valuers Registration Board of New Zealand held that he had been working totally outside the scope of his training and experience. The valuer was found negligent premised on lack of adequate knowledge of the subject market and the required expertise in valuing urban properties.

### *2.6.4 VALUATION ACCURACY*

Valuation inaccuracy particularly over-valuation, is at the heart of the bulk of professional negligence charges against real estate valuers. While the goal of the valuer is to predict what the market would offer for a given interest in a property; regretfully, there are persuasive conceptual and empirical grounds to suggest that uncertainty is inherent in the valuation process such that valuations may not be able to fulfill the intended role reliably and creditably. Inaccuracy in valuation has therefore been taken more or less as lore within valuation confraternity. For instance, the RICS once remarked that "the valuer and most informed users of valuation recognized that there will be a degree of uncertainty attached to the figure provided (RICS, 1994). Millington (1985) cited the fundamental characteristics of property as an asset class, the imperfection of the property market, the lack of central register of sales, the individual characteristics of buildings and confidentiality of information, as factors precluding valuation accuracy. In Singer & Friedlander Ltd v. John D Wood & Co, (1997) Watkin J. of a UK court held that:

"*…the valuation of land by trained, competent and careful professional men is a task, which rarely, if ever admits of precise conclusion. Often beyond certain well-founded facts so many imponderables confront the valuers that he is obliged to proceed on the basis of assumptions. Therefore, he cannot be faulted for achieving a result, which does not admit some degree of error. Thus, two able and experienced men, each confronted with the same task, might come to different conclusions without any one being justified in saying that either of them has lacked competence and reasonable care, still less integrity, in doing his work…….. Valuation is an art, not a science. Pinpoint accuracy in the result is not therefore to be expected by he who requested the valuation*".

Notwithstanding this consensus within and amongst the court, professionals and the academia; the court has tried to set limits beyond which the valuer may be considered negligent by what is popularly referred to as the "margin of error" concept. In Singer & Friendlander Ltd. v. John D. Wood & Co. (1977) which is regarded as the birth place of the principle of "margin of error", the judge was of the opinion that:

" *any valuation falling outside of what I shall call the "bracket" bring into question the competence of the valuer and the sort of care he gave to the task of valuation…………. there is, as I have said, a permissible margin of error, the "bracket" as I have called it. What can probably be expected from a competent valuer using reasonable skill and care is that his valuation falls within this bracket".*

With this and similar rulings, it would seem that the courts, particularly in the UK and Australia, may have unanimously accepted the concept of the "margin of error" as a yardstick for determining negligence (Crosby, 2002; Bretten & Wyatt, 2002; Parker, 1998; Shampton, Waller & Waller, 1998). Nonetheless, what constitutes the acceptable size of the bracket and the exact role the "margin-of-error" concept is expected to play in negligence cases remains unsettled.

Hager & Lord (1985) whose work provoked much of the later works on valuation accuracy anticipated a range of about 5% either side of the "correct" value as a reasonable margin, while Baum & Crosby (1998) suggested a "margin of error" of up to 15%. In a study undertaken by Parker (1998) among major valuation consumers in Australia, the acceptable bracket was 5% to 10% with a mode of 5% and an arithmetic mean of 6.04%. In Singer & Friedlander v. John D Wood & Co. (1977), a permissible "margin of error" of 10% either side of the "correct" figure and up to 15% in "exceptional circumstances" was adopted. Also in Trades Credits Limited v. Baillie Knight Frank (NSW) Ltd (1985) expert evidence indicated a margin of up to 15%, while in Private Bank and Trust Co. Ltd v. S. (UK) Ltd (1993) the trial judge accepted a permissive margin of error of 15% either side.

In a review of 30 UK High Court cases in which the margin of error has been an issue, Crosby et al., (1998) noted, among others, that 75% of decisions fall within 10-15% bracket and none are beyond 20%. In their study on stakeholders opinion of the acceptable "margin-of- error" in a loan security valuation, Bretten & Wyatt (2002) found that 40% of the respondents considered ± 10% as permissible, 36% of investors suggested that the bracket should not be more than ± 5%, while 25% of the valuers felt ± 15% was acceptable. None of the respondents suggested a figure exceeding ± 20%. In a similar study, Harvard (1999) found that 58% of respondent valuers thought that ± 5%-10% was an appropriate valuation range for a typical, relatively simple standing investment property. In Nigeria, Aiyedun et al., (2011) found that majority of banks (47%) and property companies in Lagos metropolis chose a margin of between 1 and 5%. Parker (1998) believes that the nature and type of property involved in each case are responsible for the differences in the acceptable margins of error.

Another unsettled issue about the 'margin of error' principle is the exact role that it is to play in negligence cases. While the limits set for the bracket has been inconsistent, the exact role of the concept in negligence cases has been more controversial (Crosby, 2002). For now, there are three different manners in which the courts have tended to employ the "margin of error" concept for decision-making in negligent cases.

First, majority of courts, especially in the UK, have treated the 'margin of error' as the sole determinant of negligence such that a valuation outside the bracket is taken as prima facie evidence of negligence. In Singer & Friendlander Ltd. v. John D. Wood & Co. (1977), it was ruled, inter alia:

"*I do not accept that where the figure under attack has been shown to be outside the acceptable bracket, the plaintiff has the additional burden of showing why the valuer reached that result".*

Again in Lewisham Investment Partnership Ltd v. Morgan (1996) the judge ruled, inter alia that:

*"Even if the defendant was not negligent in respect of any specific allegations, the plaintiff could still succeed on the basis that his overall figure was outside the permissible bracket".*

The second manner in which the concept of "margin error" has been used was to treat the concept as a ' necessary but not sufficient' condition in establishing negligence. That is, the courts require additional corroborating evidence of error of judgment especially in the construction of the valuation before negligence can be established. That is the concept of 'margin of error' is used as 'early warning' only.

A third manner the concept of margin of error is employed is illustrated by the following three cases where obvious procedural errors is considered immaterial provided the valuation falls within an acceptable bracket. In Lewisham Investment Partnership Ltd v. Morgan (1997), where the judge concluded that:

*"If I were to conclude that the defendant was negligence in respect of one or more of the specific allegations, it would still be necessary to consider whether his valuation fell within the permissible bracket because, if it did, the defendant would still escape liability".*

In Mount Banking Corporation Ltd v. Bran Cooper & Co 91992) it was stated that:

*"If the valuation that has been reached cannot be impeached as a total, then however erroneousthat method or its application by which the valuation has been reached, no loss has been sustained".*

In South Australia Asset Management Corporation v York Montague Ltd (1996), the judge marked that:

*"The valuer would not, in my view, have incurred any liability if one or more of his comments had been wrong but the valuation was correct".*

In summary, while the "margin of error" concept is fundamental to court decisions in negligence cases as typified by the UK and Australia cases reviewed above, its exact role and application is still unsettled. As Crosby (2000) remarked, the role of the bracket (margin of error) is unclear.

## *III . CONCLUSION AND RECOMMENDATIONS*

The paper addressed real estate valuers' liability for negligence in mortgage valuation. In particular, the paper sought to define the nature and extent of valuers' duty of care; and also considered such matters as contributory negligence, penalty for negligence; and the 'margin-of-error' concept. By examining case laws which addressed this problem, the paper sought to establish the legal grounds for valuers' liability while providing valuable insights into the thinking of the court in negligent valuation cases. Case law has remained the essential source for obtaining an understanding of the law relating to professional liability of valuers in negligence by providing information on the court expectations in the light of the overall "reasonable care and skill" concept, the standard by which valuers' work, like that of other professionals, are to be measured (Foster, Lavers and Waddell,1998). As such, valuers are well advised, in their own interest, to keep abreast of court pronouncements in litigations relating to their calling.

The misgivings surrounding the concept of "margin of error" notwithstanding, it may be rightly presumed that the courts will continue to apply the concept in negligence cases against valuers. By adopting this concept, the courts have sought to set the critical limits outside which valuation is regarded as misleading and the valuer is thereby liable for negligence. The court also expects the methodology and the entire valuation construction process to be logical, traceable and defensible. High level of variance or inaccuracy suggests that property investment performance cannot be reliably assessed using valuation-based indices. Valuation inaccuracy or variance would therefore adversely affect the credibility of the valuer, the reputation of the valuation profession, and damage investor's confidence in the property market. The study is therefore a clarion call on Nigerian valuers to employ more resourceful approach in mortgage valuation and to hone their skills and tools with a view to achieving acceptable levels of valuation accuracy.

Both the valuers' training and the valuers' published professional practice standards and ethics provide sufficient safeguards against liability for negligence if valuers would take time to acquaint themselves with these provisions and adhere strictly to them. For instance, valuers are mandated to decline valuation instruction for which they are not capable by training and experience, and should not accept instruction to carry out valuations in unfamiliar market. Valuers are to insist on the terms of the engagement or instruction being explicitly documented; and the limiting conditions and contingencies or assumptions on which the valuation is arrived at. Valuation firms are encouraged to put in place effective quality control system that would ensure that only diligently prepared and proven valuations pass through the system. This may include ensuring that all valuations pass through the desk of senior valuers with several years of experience; that valuation are carried out by qualified and experienced valuer; that valuation reports are discussed on the floor of the valuation unit or department before they are sent out of the system; and that the firm maintains an up to date database. Where technical specialists are brought in to assist the valuer in certain specialized area of a valuation assignment, the valuer is expected to include in the valuation report the reputation, competence, and the degree of independence of such specialists, including how the contribution of the specialists has influenced his valuation opinion. These standards and guidance notes are provide, among others, the framework for the delivery of credible valuation opinions by suitably trained valuation professionals acting in an ethical manner (IVSC, 2011).

The lessons from the UK and other Commonwealth countries cited in this study are clear and instructive. By generating awareness on the potential dangers of misguided mortgage valuations, the study provided timely caution to inept and careless valuers. The study is also expected to promote the development of local standards and benchmarking including international best practices. The ultimate goal is to protect the interest of individual valuers; preserve the integrity and future of the valuation profession; sustain the confidence of valuation users generally; promote investors' confidence in the workings of the property market; and ultimately contribute to the development of a robust mortgage system in Nigeria.

## References and notes:


**Ajayi, C. A. (2009).** International Valuation Standards as Applicable in the Use of the Investment Methodof Valuation and in Mortgage Valuation. Valuations in the Residential Property Market in Lagos. *The Estate Surveyor and Valuer , 21* (2)

**Babawale, G. K. (2007).** Valuers' Liability For Negligence. *The Estate Surveyor and Valuer, 30(1): 49-55*

**Baum, A and Crosby, N (1998):** Property Investment Appraisal Routledge, London.

**Bretten, J and Wyatt, P (2002)**. Variance in Property valuations for Commercial Lending RICS Foundational 4 (9)

**Brownell, A. (2000).** Negligence and the Valuation Industry in the Year 2000. www.prres.net/papers/Brunell_NEGLIGENCE_AND_THE (Retrieved July14, 2012)

**Bowles. McAlister & Tarbert,H. (2001)**. An Assessment of the Impact of Valuation Error in Property Investment Finance Measurement, Journal of Property Investment and Finance, (2), 139-157.

**Brown.G. (1991)**. Property Investment and the Capital Market, London: E& FN Spon.

**Crosby, N., Lavers, A., and Murdoch, J. (1998a).** Property Valuers' and Apprais' Liability Exposure: An International Perspective on Negligence in Valuation. www.prres.net/.../_Propery_Valuers_Appraisers,_Liability (Retrieved July 14, 2012)

**Crosby, N. (2000)** . Valuation Accuracy, variation and Bias in the Context of Standards and Expectations. Journal of Property Investment and Finance, 18(2).

**Crosby, N (2002):** Valuation Accuracy, Variance and Bias in the Context of Standards and Expectation. *Journal of Property Investment & Investment & Finance* 18(2) 130-161.

**Crosby, N., Murdoch, J., and Lavers, A. (2002)** "Expert valuation witnesses in the UK – problems and solutions", *Journal of Property Investment & Finance,* Vol. 20 (4), pp.316 – 353.

**Foster, H, Lavers, A. and Waddell, M (1998**). A Database of Negligent Valuation Cases and Literature. *Journal of Property Valuation & Investment,* 16(1), pp.87-98.

**Hager, D. Lord, D (1985).** The property Market, Property Valuations and Property Performance Measurement. *Institute of Actuaries,* London.

**Harvard, T.M. (1999**). Do Valuers Have a greater Tendency to Adjust a Previous Valuation Chartered Surveyors Foundation Research Paper Series 4(1)

**IVSC, (2003).** International Valuation Standards (6th Ed.), International Valuation Standards Committee, London.

**IVSC,(2011)**. International Valuation Standards, International Valuation Standards Committee, London.

**International Valuation Standards Committee. (2007).** *International Valuation Standards.*London:

**Kodilinye, G. and Aluko, O. (2001).** The Nigerian Law of Torts. Spectrum Books Ltd. Ibadan, Nigeria

**Murdoch, J. (2001).** Negligent Valuers' Liability for Market Losses in the UK & Australia. Being a Paper presented at the 7th Pacific Rim Real Estate society Conference, Adelaide 21-24 January 2001

**Murdoch, J. (2002)**. Negligence in Valuations and Surveys, 2 nd Edition. London, RICS Pubications

**NIESV (2006).** Valuation Standards and Guidance Notes of the Nigerian Institution of Estate Surveyors and Valuers, Nigeria.

**Norman A. K.**, The Ambit of Liability of Professionals for Negligent Advice or Information: The Law in Great Britain and Australia. http://www.nigerianlawguru.com/articles/torts/NEGLIGENT%20MISSTATEMENTS.pdf.

**Parker, D. (1998).** Valuation Accuracy- An Australian Perspective *Journal of Property Investment & Finance*, 17(4), 40-41.

**RICS, (1997)**. Surveyors Acting as Expert Witness: Practice Statements and Guidance Notes, Royal Institution of Chartered Surveyors, London.

**RICS (2010)**. RICS Valuation Standards (6th ed.), Royal Institution of Chartered Surveyors, London.

**Shampton J.F, Waller, T.H. & Waller, N.G. (1998).** Appraisal Malpractices: Sources of Liability and Damages. *The Appraisal Journal* Pp 399-405.

**Waldy, B. (1997).** Valuation Accuracy, Paper Presented at the 6th FIG Permanent Committee Meeting and International Symposium, Singapore.

**Wyatt, P. (2003)**. How much wrong is right? Variance in Commercial property valuation. http.www.rics.foundation.org.

## LIST OF CASES

Abbey National Mortgage Olc. C. McCormick & Merrifield (1996,unreported).
Arab Bank Plc V. John Wood (Commercial) Ltd (1998) EGCS 34
Aura Financial Services Canada Ltd v ]akubiec [1990] 22RPR 219,
Bangue Bruxelles Lambert SA. V Eagler Start Insurance Co Ltd & Others (1994) 31EG 68 and 91994) 32EG89.
Baxter V. FW Gapp & Co Ltd (1939) 2KB271.
Civil Liability Act 2003- Queensland Legislation
Coleraine Holdings Ltd v Harvey Fulton and Long [1994] NZVJ March 41
Corisand Investment v Druce and Co (1978) 248 Estate Gazette 315, 407, 504
Craneheath Securities v York Montague (1994) 1 EGLR 159
Craneheath Securities v York Montague (1996) 1EGLR 126
Donoghue v Stevenson (1932) A.C. 56:597
Graham v Pimr, Garmrm [1985] A.N –B No. 532(QB),
Kenny & Good Pty Ltd v MGICA (1996) 140 ALR 313(Known as MGICA)
Legal & General Mortgage Services Ltd V. PHC Professional Services (1997, unreported).
Lewishan Investment Partnership Ltd V. Morgan (1996).51EG75.
Mortgage Bank Plc V Edward Erdman Group Ltd (1996) 1 EGLR142.
Mount Banking Corporation Ltd V.Brain Cooper & Co. (1992) 2 EGLR 142.
Perry v Sidney Phillips and Son [1982] 1 All ER 1005
Private Bank and Trust Co. Ltd V S (Uk) Ltd (1993) 1 EGLR212.
Singer & Friedland Ltd V John D Wood & Co [1997]2 EGLR 84
Smith V, Eric S. Bush [1989] 2 WLR 790 (Court Decision No. 9)
South Australia Asset Management Corporation V York Montague Ltd (1996) 27EG 125.
Trade Credits Ltd V Baillien Knight Frank (NSW) Ltd (1985)
Trade Credits Ltd V Baillieu Knight Frank (NSW) Ltd (1985) Aust. Torts reports 80 757.
UCB Home Loan Corporation Ltd V. Roger North and Associates (1995) EGCS 149.
Zubaida V. Hargreaves (1995) IEGLR 127.

## Summary

## Valuers' Liability in Mortgage Valuation


**Gabriel K. Babawale**

*University of Lagos, Nigeria*

Valuation is a profession; valuers' clients are therefore justified in expecting valuations that meet the standards prescribed by relevant professional body(s).Failure to meet these standards constitute a source of breach of the duty that valuers owe their clients. The courts too have always looked up to the published standards of professional bodies for judgment guidelines in liability cases of contract, fraud and negligence. Drawing inferences from standards prescribed by valuers' professional bodies and ensuing mortgage valuation case laws, this study sought to establish, among others, the nature and extent of the duty of care that valuers owe their clients; the grounds for liability for negligence; the penalties for negligence; and also proffered practical steps and procedures to preventing liability for negligence in mortgage valuation. Due to the present paucity of documented pronouncements on the subject in Nigerian courts, the paper focuses on case laws in countries with similar jurisprudence, particularly Britain and other Commonwealth countries. Interestingly, decision in the British courts has often become precedents for the rest of the common law world. The ultimate goal is to help Nigerian valuers hone their skill in mortgage valuation in the light of global best practices.

**Key Words**: *case laws, liability, mortgage valuation, negligence, professional standards*