



BEST PRACTICES – EXAMPLES FROM THE FIELD

A COLLABORATION BY THE VOLUNTEER MEMBERS OF THE APPEAL SUB-COMMITTEE:

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**"IF AN APPRAISER
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TO RELY ON OWNER/
CLIENT-SUPPLIED
INFORMATION, THIS
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THAT THE APPRAISER
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SUPPORT HIS OR HER
DECISION TO RELY ON
THIS INFORMATION."**

Owner-supplied information: proceed with caution

In providing their services (appraisal, review, consulting and reserve fund studies) members of the Appraisal Institute of Canada (AIC) often rely on owner-supplied information (this could also read ‘client-supplied information’ when the client is not the owner). The information in question will generally pertain to the subject property and may include a summary of rental income, expenses, improvements, etc. This type of information may be supplied in either verbal or written form. Is there a problem with the use of owner/client-supplied information? The answer to this question, like many appraisal service related issues, is ‘maybe’ and ‘it depends.’

Referring to the Appraisal Standard Rules (ASR) listed in the 2014¹ edition of the *Canadian Uniform Standards of Professional Appraisal Practice (CUSPAP)*, we know that, in an appraisal report, an appraiser must: “identify the scope of work necessary to complete the assignment” (ASR 6.2.4). In the related Appraisal Standard Comments (ASC), this rule is elaborated upon as follows:

- The scope of work applied must be sufficient to result in opinions/conclusions that are credible in the context of the intended use of the

appraisal. The appraiser has the burden of proof to support the scope of work decision and the level of information included in the report. (ASC 7.5.2)

- The appraiser must take reasonable steps to ensure that the information and analyses provided are sufficient for the client and intended users to adequately understand the rationale for the opinion and conclusions. (ASC 7.16.1)
- In the process of collecting and verifying relevant information, the appraiser must perform this function in a manner consistent with ‘Reasonable Appraiser’ standards. (ASC 7.16.2)

So, how does the issue of owner/client-supplied information relate to the scope of an appraisal report? Referring to ASC 7.5.2, we know that the opinions/conclusions in an appraisal must be credible and that an appraiser has a burden of proof to support the level of information included in a report. Therefore, it follows that, if an appraiser makes a decision to rely on owner/client-supplied information, this information must result in opinions/conclusions that are credible and that the appraiser must be able to support his or her decision to rely on this information.

With the requirements of *CUSPAP* in mind, is it possible for an appraiser to rely on owner/client-supplied



information and still produce an appraisal where the opinions/conclusions are credible? I believe the answer is certainly, but remember the onus is on the appraiser (acting in the manner of a ‘Reasonable Appraiser’) to support his or her decision to rely on this information.

According to the 2014 edition of *CUSPAP*, a ‘Reasonable Appraiser’ is defined as:

...an appraiser who provides appraisal, review, consulting and reserve fund planning services within an acceptable standard of skill and expertise, and based on rational assumptions.

Therefore, what are some of the best practices that a ‘Reasonable Appraiser’ could employ to ensure that the owner/client-supplied information will produce an appraisal where the opinions/conclusions are credible? The most obvious one would be the application of due diligence in the form of independent verification of at least a sample of the information that is supplied by the owner or the client. For example, if the owner has provided a rent roll, the appraiser could verify the rents paid by interviewing the lessees/tenants during the inspection of the property. Further, if the owner has provided a summary of expenses incurred in the operation of the property, the appraiser could verify the expenses at source, e.g., check the cost of the electricity consumed over a year with the local utility. Note that the appraiser may require the owner’s written permission to access such records.

In summary, it may be perfectly acceptable for an appraiser to rely on owner/client-supplied information in the process of preparing an appraisal/review/consulting/reserve fund study report. However, it is important for the appraiser to proceed with caution and apply due diligence when it is appropriate. Also, the reader needs to be clearly informed of what the appraiser did or did not do (or was not able to do) in relation to the verification of owner/client-supplied information. Remember, it is mandatory for an appraiser to produce

a report where the opinions/conclusions are credible and the appraiser must be prepared to support his or her decision to rely on any owner/client-supplied information. Members of the AIC may also wish to refer to the *Professional Excellence Bulletin* found at: <http://www.aicanada.ca/wp-content/uploads/PEB-Data-verification-EN.pdf>

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Time to re-visit our measuring practices

While not the sole determinant of value, the liveable floor area (LFA) square footage of a residential home is an integral part of value. Often, I have heard members say, “why measure” when I have the LFA as reported on MLS or the municipal figure? Well, if those figures are incorrect and the appraiser did not at least try to verify the size by obtaining a Building Location Surveyor’s Certificate or performing some form of onsite measuring, he or she will be held accountable for an error someone else made.

Here is an example. A municipality quoted a home as being 1,236 square feet in size. That size was relied upon by the Realtor on MLS. While appraising the home for financing, the AIC member hand-measured the home and found it to be 1,018 square feet. This was then confirmed by a Surveyor’s Building Location Certificate and a second visit to the property to be 100% certain. The member advised his client about the discrepancy and the client alerted the purchaser and agents involved. The purchasers waited for the conclusion of the appraisal before deciding how to proceed. Had the member relied on the MLS and municipal data, the member would have erred by 21.4% in the reporting of the liveable floor area.

In another recent case, a member solely relied on the LFA reported by a Realtor for an apartment condominium.

The Realtor and the assessing body differed by 10%, with the latter being lower, but still not correct. The registered condominium plan indicated that the true LFA, as per the condominium declaration, was, in fact, 20% lower. The Realtor thought he had used proper measuring guidelines. The assessing body confirmed that they had not been able to inspect the unit and had made some assumption in their calculations. No attempt had been made by the member to either measure the unit or obtain the condo plan. If the error had not been discovered, a serious over-valuation could have resulted.

Members are advised to pay particular attention to condominium property, since measuring practices can vary from province to province (or territory) and sometimes from project to project.

Appraisers are retained to provide their professional estimate of market value by relying on a professional assembly of the facts. It is incumbent on appraisers to confirm what is being reported. Sometimes, it is not easy to measure contemporary designed homes from the exterior. Appraisers should at least try to verify LFA by measuring the footprint of the building, measuring the upper floors of the interior, or obtaining a building location certificate or a set of blueprints. There are many devices available that a member can use to measure (the trusty 50- or 100-foot measuring tape, laser devices, etc.). It is also important for the appraiser to disclose what he or she was or was not able to verify, to state the source of what was relied upon, and to invoke all relevant assumptions and limiting conditions.

Depending on the type of real estate being valued, the appraiser should be very familiar with AIC guidelines. AIC has extensive advice on measurement in the Member’s section of its website at: <http://www.aicanada.ca/professional-practice/measurement-practices/> Members can also refer to the BOMA guidelines for non-residential properties.



One cannot go wrong by carrying out some form of onsite measuring. This little bit of added time today could save an appraiser countless hours of time in the future, if his or her report were ever called into question.

CUSPAP² linkages:

Appraisal Standard Rule 6.2.9 – In the report, the member must identify the location and characteristics of the property and the interest appraised.

Appraisal Standards Comment 7.5.2 – The scope of work applied must be sufficient to result in opinions/conclusions that are credible in the context of the intended use of the appraisal. The appraiser has the burden of proof to support the scope of work decision and the level of information included in a report.

Appraisal Standards Comment 7.10.1 – Characteristics of the Property [see 6.2.9, 14.20, 14.28] – Relevant to the purpose and intended use of the report, characteristics of the property must be analyzed and included in the report, including but not limited to physical, legal and economic attributes.

Members are reminded that, under Ethics Standard Rule 4.2.3, it is unethical for a member to knowingly act in a manner that is misleading (and Comments 5.3.1/5.3.3).

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Prospective value – or not?

Some members struggle with the concept of when their valuations should be labeled as ‘prospective’ estimates. Most often, this relates to new construction, where the value being sought is ‘as-if-complete.’ By introducing the Extraordinary Assumption (i.e., that construction is complete), some members interpret this as providing a prospective value. That is not usually the case.

Discussion of this concept is found in Appraisal Standard Comment (ASC) 7.63 of *CUSPAP 2014*³. A Prospective Value Opinion:

“refers to an effective date following the date of the report; it is a forecast..... Prospective value opinions are intended to reflect the current perceptions of market participants as to the future.”

When an assignment requires an Extraordinary Assumption that the property is complete, it should treat the property as if it exists at the time of analysis. Just like an existing property, the analysis reflects a snapshot of the market today, using recent sales to formulate the value opinion. The appraiser should think of it as being the same as inspecting a property – only that an understanding of the property is being assembled from blueprints and specifications. The assumption is that the property exists today, and it is being valued today.

This does not usually require a forecast of changes in the market over the course of the construction process. A prospective value does require such a forecast, and thus the reference to a future ‘effective’ date.

Prospective values can be required for projects that will take a period of months or even years in order for the circumstances to arise for which the appraiser is making the forecast. For example, a project such as an assisted living seniors’ complex might be valued ‘as of the date of stabilized occupancy.’ If the task of the appraiser is to value the property as of that future effective date, then the likely changes in the market must be analyzed and their effects incorporated into the analysis. It is distinct from the premise that the property exists, as of the effective date, and thus is subject to known market conditions at the date of analysis.

The requirement for a Prospective Value is a scope of work issue and should be discussed with the client, (or the intended user, if appropriate and with the client’s consent) so that it is clearly

understood the analysis will account for expected changes in market conditions. Getting back to ASC 7.63, this must be made clear in the report:

“The use of clear language and consistent terminology in a prospective report (i.e., future tense throughout) is necessary for the reader not to be misled...”

As a side note, appraisals ‘as-if-complete’ usually require introduction of both Extraordinary Assumptions and a Hypothetical Condition. The Extraordinary Assumption covers the physical side of the assignment – issues like the size of the building, the quality of construction and the type and quality of finish. These are usually matters that are defined in the blueprints and specifications. The Hypothetical Condition is in assuming the building exists, when it is known to vary from fact (i.e., the house does not yet exist), and is introduced strictly for purposes of ‘reasonable’ analysis. To put this in perspective, think of a situation where the proposed building is never built. This does not make the report wrong or misleading – however, members should be aware that, technically, they invoke both Extraordinary Assumptions and Hypothetical Conditions in completing this type of work, and should explain to the reader that both elements are incorporated in their opinion(s).

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End notes

- 1 At time of writing, *CUSPAP 2014* was still in effect. Members are reminded to refer to *CUSPAP 2016* for the complete list of professional services and the mandatory requirements for any assignment completed on or after May 1, 2016.
- 2 Ibid.
- 3 Ibid. 