

Extraordinary or not?



Unravelling the use of special exclusions and limitations in appraisal reports

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The use of Extraordinary Assumptions, Extraordinary Limiting Conditions, Hypothetical Conditions and Jurisdictional Exceptions in our appraisal reports has long been, in my view, an under-taught, under-utilized and often misapplied part of our practice as appraisers. This is a serious problem as their correct use can literally make or break your appraisal report, impact its effectiveness, and determine success or failure in the defence of your report should it be challenged.

Over my 3½ decades of writing and reviewing appraisal reports, this is a noted area of weakness in many appraisal reports. The *Canadian Uniform*

Standards of Professional Appraisal Practice (CUSPAP) is where these tools are introduced and explained. However, *CUSPAP* can be confusing, unclear, and, at times, seemingly contradictory in its advice around the use of these critical statements. For this article, 'Extraordinary Assumptions, Extraordinary Limiting Conditions, Hypothetical Conditions and Jurisdictional Exceptions' will collectively be referred to as 'ELCs+.'

This article aims to identify the definitions and examples of each of these four exclusions and highlight areas to help demystify their correct use. To be clear, this is solely an introduction and not an all-encompassing review of all

possible scenarios that may require use of one or more of these ELCs+, thereby reducing liability (for both individual Members and AIC).

INITIAL CONSIDERATIONS WHEN DETERMINING WHAT TO INCLUDE IN APPRAISAL REPORTS

Think about the authorized use of the report. Does the report truly align with and support the client's use of the report? Does the report make sense for the authorized use? Does it pass the 'sniff' test? Are the assumptions reasonable based on the use of the report? Are they extraordinary? Could there be anything potentially misleading about the report for the authorized use?

HUMBLING BACKGROUND

The very first statement in the *CUSPAP 2024* document reads:

Compliance with CUSPAP

Compliance with the requirements of all components of CUSPAP is mandatory for all types of Professional Services Assignments.

Professional Services Assignments include the following: *Real Property Appraisal, Review, Consulting, Reserve Fund Study, Machinery and Equipment Appraisal, and Mass Appraisal.*

That is seriously unambiguous – a sobering thought when considering that you can be denied liability insurance coverage if your report is found to be non-compliant with *CUSPAP*.

There are associated ‘Standards’ sections in *CUSPAP* for each of these professional services, plus one other: the Reporting Standard. This means that, if you are preparing an appraisal or a consulting assignment, there are at least two Standards to which you must comply (Reporting and Appraisal Standards or Reporting and Consulting Standards in this example). The Ethics Standard contained within *CUSPAP* also applies to everything we do, not just preparing reports.

Another statement in *CUSPAP 2024* reads:

Legislation and/or Regulations

Members are required to comply with the applicable legislative and/or licensing requirements for all types of Professional Services Assignments.

Legislation supersedes CUSPAP.

It is evident that strict compliance with *CUSPAP* and legislation is essential. Avoiding common mistakes and risks – particularly those related to *CUSPAP* compliance, such as ELCs+ – is a critical part of meeting these requirements.

BREAKING DOWN THE MEANING AND INTENT OF ELCs+

Digging into the specifics for each type of limitation, exclusion or assumption

included in the global ELCs+, and providing definitions, explanations and examples of each type, we can look to *CUSPAP* for some initial guidance on the appropriate (or inappropriate) use of these special statements in our reports:

5.2.1 *It is unethical for a Member to develop, use or permit others to use, for any purpose, any report which the Member knows, or ought to know, is defective, erroneous, and/or misleading.*

7.9.4 *Before invoking an Extraordinary Limiting Condition, the Member must determine that the Scope of Work applied will result in analyses, opinions and conclusions that are credible and will not be misleading.*

7.10.8 *An analysis based on a Hypothetical Condition must result in a credible analysis and must not result in a report that is misleading.*

Although not specifically stated in *CUSPAP*, these qualifications apply equally to all special statements within the ELCs+ sphere. ‘Misleading’ is the common theme. Members must never produce a report that we know, or ought to know, is misleading.

Most often, the issuance of a potentially misleading report is not intentional. To help avoid this, step back and consider objectively the ‘initial considerations’ in this article and apply them when considering an assignment and its content.

EXTRAORDINARY LIMITING CONDITIONS

The *CUSPAP* definition of Extraordinary Limiting Conditions reads:

3.29 *A necessary modification or exclusion of a Standard Rule which may diminish the reliability of the report.*

This sounds simple enough. In preparing a report, if Members do anything outside the specific requirements of any of the eight Standards in *CUSPAP*, then they must invoke an Extraordinary Limiting Condition. Why might one ignore or modify a Standards rule?

Some examples include lacking an interior inspection of the subject improvements, excluding an approach to value that the Reasonable Appraiser would typically undertake, ignoring the scheme in an expropriation appraisal, not completing a title search, or lacking liability insurance if the property is outside of Canada.

CUSPAP further states:

7.9.5 *The Member must include an explanation and justification of Extraordinary Limiting Conditions in the Report.*

9.3.2 *A Member must personally inspect the subject property or identify an Extraordinary Limiting Condition if they did not.*

EXCLUSION OF AN APPROACH TO VALUE: (IS IT EXTRAORDINARY?)

There are two issues here (and for other potential ELCs); is it in fact ‘extraordinary’; and if so, what is the correct and compliant application and explanation of the ELC.

CUSPAP states:

Excluding an approach to value that is relevant under the ‘Reasonable Appraiser’ test requires:

An Extraordinary Limiting Condition, and supporting reasons.

Excluding an approach to value that is not relevant under the ‘Reasonable Appraiser’ test requires:

Supporting reasons only.

In other words, excluding an approach to value that the Reasonable Appraiser would not complete (i.e., an Income Approach in a typical single-family dwelling report) is not extraordinary as far as *CUSPAP* is concerned. To be fully compliant with *CUSPAP*, the appraiser simply needs to explain that it is an approach not relevant to the assignment, and why.

Alternately, not completing an Income Approach on a rental apartment building does indeed require an ELC because the Reasonable Appraiser *would* complete it.

You need to very carefully consider excluding an approach to value that would typically be considered relevant to the assignment before invoking such an ELC. Consider if there is a valid reason to not complete the approach and if it will impair the ability to value the property based on market expectations. Is there a lack of data or of property details? Is quick turnaround time impacting the decision? Does the client not want to pay for the inclusion of this approach? Be very careful about these. A few examples follow:

EXAMPLE 1:

Excluding the Cost Approach (an ELC)

The subject property includes a newly constructed building. However, the Cost Approach has not been included at the request of the client. As this is an approach normally considered relevant to the valuation of new or newer improvements, an Extraordinary Limiting Condition has been invoked.

Real Property Appraisal Standard 8.2.8 requires an appraiser to ‘describe and apply the appraisal procedures relevant to the Assignment.’

As a result, reliance on this report may be diminished by the exclusion of the Cost Approach. Were the property to include a 70-year-old industrial building nearing the end of its useful life, then excluding the Cost Approach would not require an ELC, as neither the market nor the Reasonable Appraiser would consider this methodology to determine price/value.

EXAMPLE 2:

No inspection of the subject property

Although attempts were made, the subject property was not inspected because of a dispute between the client and the property owner. An Extraordinary Limiting Condition has been invoked as a result.

Reporting Standard Rule 7.5.1.i requires inspection of the subject property and

Real Property Appraisal Standard Rule 8.2.3 requires the appraiser to ‘identify the property and describe its location and characteristics.’ As such, it is acknowledged that reliance on the results of this report may be diminished by the lack of an inspection.

This clearly constitutes an Extraordinary Limiting Condition and should be treated and discussed in the report as such. Further, because no inspection of the property was completed, this will also result in the need for further ELCs+ (Extraordinary Assumptions at minimum). The report will need to lay out what assumptions were made with respect to the subject property, for example, its quality, condition, layout, etc., and how such assumptions might impact the report. The report should also provide support for the content of your assumptions (data sources) to be valid and not misleading.

Let’s now look at Extraordinary Assumptions and how to invoke them in compliance with CUSPAP.

EXTRAORDINARY ASSUMPTIONS

CUSPAP definition:

3.28 *An assumption, directly related to a specific assignment, which, if found to be false, could materially alter the opinions or conclusions.*

Extraordinary Assumptions presume as fact otherwise uncertain information about or anticipated changes in the physical, legal or economic characteristics of the subject property, or about conditions external to the subject property such as market conditions or trends, or the integrity of data used in an analysis.

Examining the difference between this and a Hypothetical Condition can be subtle and easily mischaracterized, and the Standards must be kept front of mind.

Some examples of Extraordinary Assumptions include the absence of contamination where contamination is possible, the inspection of the property taking place after the effective date (retrospective valuations), a portion of the property not being available for inspection, municipal sanitary service availability when timing is uncertain, if the in-process zone change approval will be successful, and a prospective appraisal. Further rules from the Reporting Standard (CUSPAP 2024) state:

7.9.1 *If an Extraordinary Assumption is invoked, wherever an opinion or conclusion is stated within a Report, the Extraordinary Assumption must be stated in its entirety or a reference to its exact location in the report must be provided.*

7.9.2 *When referencing the subject matter of an Extraordinary Assumption in a report, it must be clearly indicated that the opinions or conclusions are based on the Extraordinary Assumption.*

7.9.3 *Wherever an Extraordinary Assumption is referenced in a report, it must be clearly identified as an Extraordinary Assumption.*

Professional assistance from non-member:

7.12.5 *An Extraordinary Assumption and/or a Limiting Condition regarding the Designated Member’s reliance upon Professional Assistance provided by a non-member must be included in the Certification of a report.*

EXAMPLE 3:

Condition of the property (retrospective)

The subject property was inspected on May 10, 2025, and the effective date of the report was July 1, 2023. It is assumed that no significant changes have happened to the property between the effective date

and the inspection date unless otherwise confirmed and detailed in the Report. If this assumption is found to be incorrect, it could impact the findings of market value as reported.

This is a fairly common EA in appraisal reports (particularly for those doing retrospective valuations). The key is to be clear about any changes to the property between effective and inspection dates that can be confirmed and to have that be reflected in the valuation. Rarely are properties exactly the same from one date to another, so be clear and concise in the description in the Report (as referenced in your EA).

EXAMPLE 4:

Land use amendments

The subject property is currently zoned MR-2. As of the effective date of the valuation, the property owner has submitted a zone change application seeking increased density with MR-3 zoning (such approval is considered probable). The report and its findings are based on the assumption that the MR-3 zoning will be approved (see 'Land Use Controls' starting on Page 43 for further discussion). Without this assumption, the findings of market value within the report could be different.

Breaking this down, when invoking such an assumption, it must be clear that the anticipated change to the zoning of the property and the resulting increase in development density is indeed probable (think Highest and Best Use – probable versus possible). Further, dealing with this assumption from a valuation perspective is as important as the EA itself. How do you reflect the potential increase in density in the current valuation? A prospective valuation could be an option, but this will result in a different value than examining the current value of the potential. It can be subtle, but very important to get right. Again, what is the objective of the client? It must all align and be consistent.

EXAMPLE 5:

Absence of contamination

The subject property is located in the vicinity of known environmental contamination sources and may be impacted. An environmental impact survey has not been completed on the property as of the effective date of the report. For the authorized use of the report, it is assumed that the subject property is not negatively impacted by contamination detrimental to its value.

If this assumption is found to be incorrect, it could impact the findings of market value as reported. Any liability for the impact of potential contamination of the subject property is expressly denied by the appraiser.

In this scenario, it would be ideal (and strongly advisable) that this Extraordinary Assumption was as mandated by the client in writing and should be referenced as such in the EA. This leaves no doubt as to the reasons for the appraiser making the assumption. If, however, the authorized use is for a purpose where possible contamination should indeed be considered (think valuation of assets for a divorce proceeding for instance), the client's urging to ignore it may not be sufficient and could lead to the issuance of a misleading report.

EXAMPLE 6:

Municipal sanitary service

Development of the subject property for residential subdivision purposes is dependent upon the availability of municipal sanitary service. As of the effective date of the valuation, it is uncertain when sanitary service will be available to the property. Through consultation with the local municipality and the developer (refer to 'Servicing' discussion, Page 54), it has been assumed for reasonable analysis purposes that sanitary sewer services will be available in approximately five years

(from the effective date). Without this assumption, the findings of market value within the report could be different.

For those valuing development land, the timing and availability of services is key to value in most instances. For analysis purposes, we need to make a reasonable assumption about these services in consultation with local municipalities, engineers, developers and other sources of support for these estimates.

To convey to your client and users of the report that there is a reasonable range of potential outcomes (servicing availability) leading to a range of potential current values depending on the overall consensus of concerned parties on this critical timing, a sensitivity analysis within the report could be considered. Again, consistency and clarity in terms of the research, assumptions, and their potential impact to the valuation is key in minimizing the potential liability from such a report.

HYPOTHETICAL CONDITIONS

There is significant potential cross-over between Extraordinary Assumptions and Hypothetical Conditions and they can often be confused. Examining the critical difference between them and reviewing some examples aims to bring some further clarity.

CUSPAP definition:

3.3.6 Hypothetical Conditions are a specific type of Extraordinary Assumption that presumes, as fact, simulated but untrue information about physical, legal or economic characteristics of the subject property or external conditions, and are imposed for purposes of reasonable analysis.

Reading this and the EA definition again, the key when making an EA versus a HC, is the distinction of the assumption being

presumed but uncertain versus *presumed but untrue*.

CUSPAP Section 7.10 of the Reporting Standard provides some further clarification and requirements when invoking Hypothetical Conditions. It is strongly recommended to review this section of CUSPAP whenever invoking an HC is a consideration. In summary, Hypothetical Conditions may be used when they are required for legal purposes, for purposes of reasonable analysis or for purposes of comparison. It must be clear to the reader that the property condition does not, in fact, exist as at the date of appraisal, and the analysis performed to develop the opinion of value is based on a hypothesis.

For certain valid and appropriate Hypothetical Conditions, some of the 7.10 requirements do not apply. For instance, for an expropriation report, it may be necessary to completely ignore the reality of the scheme (reason for the expropriation) to correctly value the property in law. This would make iii and iv in 7.10.5 not applicable as such cannot happen in reality. It would be good to highlight this in such a report to avoid any potential CUSPAP compliance concerns.

Further CUSPAP guidance states:

7.10.6 Reports for expropriation can require Hypothetical Conditions and may require the Member to invoke a Jurisdictional Exception.

7.10.7 The Hypothetical Condition must be clearly disclosed in the report, with a description of the hypothesis, the rationale for its use, and its effect on the result of the Assignment.

7.10.8 An analysis based on a Hypothetical Condition must result in a credible analysis and must not result in a report that is misleading.

9.10.1.i If a lease is to be disregarded and the Assignment is of the fee simple interest and not the leased fee, an Extraordinary Assumption (Hypothetical Condition) is required.

Some examples of potential Hypothetical Conditions include the absence of contamination where such contamination exists, municipal sanitary sewer when none is available, assumed residential zoning where agricultural zoning is in place, rezoning has been achieved when it has not, assumed renovated condition when renovation remains incomplete, repairs or improvements 100% complete when untrue, ignoring a lease in place and an expropriation scheme is disregarded.

EXAMPLE 7:

Absence of contamination

The subject property is known to have environmental contamination due to its proximity to a previous landfill operation in this location. Remediation of the environmental contamination from the site would likely require complete demolition of the improvements and excavation and fill of the site to allow for redevelopment of the property. Remediation costs remain unknown.

The report is completed under the hypothetical condition that there is no environmental contamination affecting the subject property for reasonable analysis purposes and for the authorized use of the report (litigation with respect to the potential contamination). The values reported herein would be different in absence of this hypothesis. An Extraordinary Assumption has been invoked as a result (may not be required).

This or similar scenarios are not uncommon and require some careful consideration before undertaking. The key

is often ensuring that the objective of your client and the authorized use of the report align without question. With many of these potential hypotheticals, they may be quite appropriate in some circumstances and entirely inappropriate and misleading in others.

EXAMPLE 8:

Municipal highway expansion

The subject property (a rural residential dwelling) is the subject of an expropriation of a portion of the site wherein the re-alignment of Highway 1 will bring the roadway very close to the dwelling. It is the hypothetical assumption for the report, for reasonable analysis purposes according to a required Jurisdictional Exception (refer to Page 23), that the re-alignment of the highway is not taking place, thereby not impacting the subject property nor its market value. Without this assumption, the findings of market value within the report could be different. An Extraordinary Assumption has been invoked as a result (may not be required).

There are many expropriation matters that legitimately require one or more Hypothetical Conditions. To ignore the law with respect to municipal takings and reporting requirements for compensation is folly. Be sure to fully understand what is required for these reports and ensure CUSPAP compliance with the use of these exclusions.

EXAMPLE 9:

Building is 100% complete

As of the effective date of the report, the subject property remains under construction and is not ready for occupancy. The analysis in the report is completed under the hypothetical condition that the subject building is 100% complete as of the effective date, at the request of the mortgagee. It is expected that the subject building will be completed within six months of the effective date based on current projections from the developer.

The values reported herein would be different in absence of this hypothesis. An Extraordinary Assumption has been invoked as a result (may not be required).

Another common scenario; a current value of the property 'as-if complete.' It is critical that any report makes very clear from the outset that the property is, in fact, not complete as of the effective date and that the value conclusions in the report are based on the hypothesis that the building is complete.

EXAMPLE 10:

House and five acres for mortgage financing

As of the effective date of the report, the subject property, as legally described, includes 100 acres of land and various agricultural outbuildings, along with a single-family dwelling. As per the request of the client (lending institution), the report values the existing dwelling on a hypothetical five acres of separately conveyable land (as described in the report) without any value contribution of the agricultural outbuildings nor any consideration of the highest and best use of the larger parcel.

The hypothetical entity as valued does not exist and cannot be created through severance as it is not currently allowed within the zoning by-law. A valuation of the entire legal entity would result in a different value conclusion and may be greater or lesser than the hypothetical entity. An Extraordinary Assumption has been invoked as a result (may not be required).

This common scenario can be a bit of a mine field and one that appraisers face on a regular basis. Although it is unlikely that the larger parcel would be valued lower than the hypothetical house and five acres, it is not impossible (think contamination in a portion of the larger parcel). It is advisable to remind the client overtly that the appraiser takes no responsibility for any positive or negative influence of consideration of the entire legal parcel.

Keep in mind also that, although the property's hog barn may be outside the hypothetical five-acre parcel, any analysis should nonetheless consider the impact of its proximity to such a potential negative influence.

As with all special exclusions, be very clear about the assumptions made and the impact of those assumptions. Be sure, equally, that this type of request aligns with the client's use of the report (i.e., this may be entirely appropriate for a mortgage financing report, but entirely inappropriate and misleading for a divorce or partnership dispute valuation).

JURISDICTIONAL EXCEPTIONS

CUSPAP definition

3.4.3 An assignment condition that permits the Member to disregard a part or parts of these Standards that are determined to be contrary to law or public policy in a given jurisdiction; only that part shall be disregarded and of no force or effect in that jurisdiction.

Jurisdiction relates to the legal authority to legislate, apply, or interpret law at either the federal, provincial, or local levels of government.

A Jurisdictional Exception must flow from legislation (Acts, Bylaws, Procedures authorized and developed from Bylaws, or case law). [see 19.8]

In a report, the Member must identify the part or parts of CUSPAP disregarded as well as provide a reference to the law, regulation or legal authority that precludes compliance and supports the Jurisdictional Exception.

It is the responsibility of the Member, not the Authorized Client or other Authorized User(s), to determine whether the use of a Jurisdictional Exception is appropriate.

Three examples of potential Jurisdictional Exceptions involve the *Expropriation Act* – Ignoring the Scheme; the *Excise Tax Act* – Self-supply for Federal GST/HST purposes; and the municipal assessment valuation – fairness.

EXAMPLE 11:

Ignoring the Scheme

As of the effective date of the report, the subject property (a rural residential dwelling) is the subject of an expropriation of a portion of the site wherein the re-alignment of Highway 1 will bring the roadway very close to the dwelling.

The Expropriation Act R.S.O. 1990, c. E.26 often requires valuations for expropriation to ignore the impact of the reason for the expropriation itself (i.e., 'ignore the scheme') when valuing assets to determine appropriate compensation; this is one such circumstance.

As a result, certain parts of CUSPAP Section 8 (Real Property Appraisal Standard) have been ignored or modified, including parts 8.2.3, 8.2.4, 8.2.5, 8.2.6 and 8.2.12.

The values reported herein could be different in absence of this Jurisdictional Exception. Associated Extraordinary Limiting Conditions and Hypothetical Conditions have been invoked as a result (refer to Pages 10 & 11).

The results of the valuation are invalid for any purpose other than for determination of compensation as a result of expropriation of the subject property.

This is an example of the detail required in a Jurisdictional Exception (JE) when legislation or policy requires us to complete an analysis or valuation differently than would normally be done. As outlined in CUSPAP, the JE must reference the legislation or policy that leads to the need to ignore or modify the Standard(s) and it must reference the Standard(s) that were ignored or modified for reasonable

analysis purposes. Best practice would be to include a statement specifically excluding the use of the report for any other purpose. Further, there will almost certainly be other ELCs+ required in the report associated with the JE that has been invoked.

Although *CUSPAP* is very clear that it is a Member's responsibility to determine the appropriateness of a Jurisdictional Exception, it is also critical to discuss this with the client in detail prior to completion of a report under such a limitation.

SCENARIOS FOR CONSIDERATION

The following are some potential situations common to AIC Members that should lead to consideration of the appropriateness of a request and which ELCs+ may need to be invoked to appropriately value a property. Talk about these with colleagues and develop appropriate verbiage (including detailed ELCs+ for the scenarios being seen on a regular basis):

- A CRA being asked to value a house on a commercially zoned site for bank financing
- Expropriation valuation for development land where no services currently exist
- Being asked to complete an appraisal absent an inspection
- A lawyer asking a CRA to appraise a 50-acre farm property for divorce settlement (Can just the house and five acres be valued if the lawyer agrees?)
- Being asked to appraise a house where a murder recently took place
- A lawyer requesting an appraisal of a contaminated industrial property
- Being requested to complete an appraisal outside of Canada
- Cosigning a report for a Candidate where the Cosigner did not inspect the property (hint: 9.3.2)
- An AACI inspecting four apartment units in a 100-unit building for mortgage financing

SUMMARY

There is a myriad of circumstances where the use of one or some combination of ELCs+ is critical to a valuation report. Equally, there are many circumstances where their use is inappropriate and can lead to the issuance of a potentially misleading report, exposing the appraiser and AIC to significant liability. Understanding this difference in reports and in practice is step one in keeping reports on track and in compliance.

Importantly, ELCs+ are not a *carte blanche* for AIC Members to make any manner of wild assumptions or hypotheticals that clients may request in order to encourage an outcome in their favour. There must always be rational, supportable, and defensible reasons for invoking any ELCs+ as provided for within *CUSPAP*.

Be sure to reference the invocation of any ELCs+ wherever a value conclusion is stated and where other critical conclusions are drawn within a report (i.e., highest and best use analysis, land use controls discussion). It is not sufficient for ELCs+ to be correct and appropriate; they must also be made very clear and obvious to the readers or users of the report.

When using these critical tools, be clear, be careful, be critical and ultimately be confident that the resulting valuation is not potentially misleading and aligns with client's use of the findings of the report. Be a devil's advocate for any personal or company report assumptions – step back and assess the use of ELCs+ coldly and objectively. Consistently employing these steps contributes ultimately to maintaining credibility as a professional; such is invaluable.

It is one (unfortunate) thing to breeze over ordinary Assumptions and Limiting Conditions in reports; it is an even more serious risk to employ ELCs+ randomly or carelessly without truly understanding the impact of their invocation on both the value conclusions and the effective and appropriate use of reports. ■