

# AMERICAN INSTITUTE OF MINERALS APPRAISERS

## NEWSLETTER

July 1996

Vol. 2, No. 1

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#### **THINK ABOUT PROFESSIONAL DEVELOPMENT**

by Michael R. Cartwright, CMA, ASA, RPG

I think I heard before that a suggestion to raise the dues always brings disheartening groans; but I'm going to bring it up once more. I really believe that we need to encourage our members to obtain the latest copy of Uniform Standards of Professional Appraisal Practice (USPAP). It costs \$25 for a one-year order, \$45 for a two-year order or \$60 for a three-year order through The Appraisal Foundation. A dues increase of \$25 per year to cover the cost of receiving USPAP from The Appraisal Foundation and repackaging and mailing it to each member does not seem unreasonable. This method will also serve to put us into a good light with The Appraisal Foundation since we are taking steps to keep our membership abreast of changes.

*Editor's Note: What are your thoughts on this? The Appraisal Foundation is, of course, important. We investigated membership for the AIMA... but the \$18,000 fee drove us away. Could we follow Cartwright's suggestion?*

I think that we may need to put a requirement into our membership requiring our members to take and pass a 15-hour course in USPAP upon first becoming a member and that they would need to take USPAP every five years thereafter in order to remain "certified". This is the standard requirement of all professional appraisal organizations and is required by The Appraisal Foundation under state licensing and certification statutes.

*Editor's Note: We are looking into the availability of a 15-hour USPAP course as well as "refreshers". Clearly, we would need to "grandfather" existing members. Would such a requirement drive away any (all?) future candidates?*

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#### **CONFIDENTIALITY UNDER THE UNIFORM STANDARDS OF PROFESSIONAL APPRAISAL PRACTICE**

Michael R. Cartwright, CMA, ASA, RPG

Confidentiality requirements under USPAP are covered in the Confidentiality Section of the Ethics Provision and in Statement 5. These provisions basically state that an appraiser is a fiduciary and must not disclose confidential factual data obtained from the client or the results of an engagement prepared for a client to anyone other than: 1) the client and persons specifically authorized by the client; 2) such third parties as may be authorized by due process of law, and 3) a duly authorized professional peer review committee. USPAP does not specifically address interpretive data (analyses, opinions, conclusions, etc.) supplied by the client or by third parties and it considers factual data supplied by third parties to be non-confidential unless specifically advised otherwise.

USPAP recognizes that factual data supplied to the appraiser by the client are to be treated as confidential only when the client specifically instructs the appraiser that the factual data are confidential. This, of course, is the exact opposite of what any reasonable person would consider to be a fiduciary duty. To the best of my knowledge the USPAP application of confidentiality is not in accordance with AIMA, ASA, AIPG, MICA, AIMR, AICPA, state geologist registration laws, and most other professional organizations ethics provisions, which operate under the assumption that unless otherwise agreed to, a consultant may not use or disclose confidential information acquired through an engagement.

According to a business law textbook confidential information means data that are valuable to the client because they are not widely known, or that would harm the client's business if they became widely known. Examples include a client's business plans,

financial condition, contract bids, technological discoveries, manufacturing methods, customer files, and other trade secrets. These examples are all items that are commonly supplied to appraisers. As minerals appraisers confidential information would include all of the above and sample location and assay/analysis data, geological/geochemical and geophysical maps, interpretations and reports, mineral exploration, resource and reserve reports, and other similar items.

USPAP justifies its anomalous confidentiality position by asserting that market data is necessary to the appraisal profession and the quality of work that the public has a right to expect from professionals. To hold that all factual data obtained from the client are confidential simply because they were given to the appraiser for use in connection with the appraisal is an extremely broad and arbitrary construction that unduly burdens the appraiser without a compensating benefit to the public. Less available data tends to diminish the quality of appraisal services.

Under USPAP the obligation of an appraiser to protect the confidential nature of the appraiser-client relationship is neither absolute nor clearly understood. The appraiser-client relationship envisioned by USPAP is not comparable to the attorney-client relationship, nor in my experience, is it comparable to a normal geologist-client relationship. With regard to factual data supplied to an appraiser by a client, USPAP indicates that the client is in the best position to decide what data must be considered confidential and to provide an explanation for such a determination. USPAP recognizes that such data are to be treated as confidential only when the client specifically instructs the appraiser that the factual data are confidential. Under normal business laws, and the Lac decision, a minerals appraiser would be better served by assuming that all data is confidential and would be best served by using a written confidentiality agreement. □

#### ARTICLE OF INTEREST IN *MINING MAGAZINE*

The July 1996 issue of the *Mining Magazine* (pages 36-38) contained a lucid and accurate article on the problem of appraising undeveloped mineral resources. Authored by H. Van Tingley whose experience covers valuation, due diligence, fairness opinions and business analysis for a New York consultant firm, the article is recommended reading for our members.

Tingley is not afraid to state that "most undeveloped resources have limited value" and "...development of some [mines] -- even most -- will not occur for years."

Also, Tingley is very frank (but not necessarily popular with a weller when he writes about undeveloped prospects "...DCF [analysis] can most safely be applied to a permitted property that has a completed feasibility study because the feasibility study and permitting process serve to reduce project risks sufficiently to enable a buyer to measure property value reasonably objectively."

We have sent Mr. Tingley a copy of the AIMA application package and hope he will join our group. *John B. Gustavson*

#### APPRAISALS AND APPRAISAL REPORTS UNDER USPAP

Michael R. Cartwright, CMA, ASA, RPG

The information in this article is based on the 1996 edition of the Uniform Standards of Professional Appraisal Practice (USPAP) and from an Appraisal Institute seminar I attended on *Understanding Limited Appraisals and Appraisal Reporting Options*.

#### Types of Engagements

Appraisers are legally regulated under federal and state law by USPAP which considers three forms of appraiser engagement by a client: appraisal, review, and consulting. **Appraisal** is the act or process of estimating value and should be used whenever the appraiser could be perceived as an independent and disinterested party. **Review** is the act or process of critically studying a report prepared by another. **Consulting** is the act or process of providing information, analysis of data, and recommendations or conclusions on diversified problems, other than estimating value.

USPAP identifies three defined activities as consulting: market analysis, feasibility analysis, and cash flow/investment analysis. Market analysis is the study of market conditions for a specific type of property. Feasibility analysis is a study of the cost-benefit relationship of an economic endeavor. Cash flow analysis is a study of the anticipated movement of cash into and out of an investment. Investment analysis is a study that reflects the relationship between acquisition price and anticipated future benefits of an investment.

#### Impartial Consulting vs. Advocacy

Differentiation among these activities depends upon the purpose and intended use of the results. USPAP recognizes two types of consulting engagements: (1) performing an impartial consulting service as a disinterested third party that responds to the client's stated objective, and (2) performing a consulting service that is intended to facilitate the achievement of the client's objective.

If third parties, or the public, would reasonably perceive an appraiser to be acting as a disinterested, objective third party, that is enough to bar the appraiser from acting as an advocate for the client in that particular situation. If a person could be reasonably perceived by others to be acting as a disinterested third party, then the assignment must be performed with impartiality, objectivity, and independence. In either event the appraiser must clearly disclose which role is being performed for the client.

#### Types of Appraisals

The scope of an appraisal engagement refers to the extent of the process of collecting, verifying, analyzing, and reconciling

relevant data. A client may engage an appraiser to perform either a Complete or Limited Appraisal. A **Complete Appraisal** is the act or process of estimating value without invoking the Departure Provision. To develop this type of appraisal, the appraiser uses all applicable approaches to value and the value conclusion reflects all known information about the subject property, market conditions, and available data.

A **Limited Appraisal** is the act or process of estimating value performed under and resulting from invoking the Departure Provision. It is a Limited Appraisal because both the appraiser and the client agree prior to the commencement of the engagement that the appraiser will not use all applicable approaches to value, or that the value conclusion will not reflect all known information about the subject property, market conditions, and available data.

### **Disclosure of Departures from Guidelines**

The burden of proof is on the appraiser to decide before accepting an assignment and invoking this provision that the result will not confuse or mislead. The burden of disclosure is also on the appraiser to clearly identify and explain any departure(s) from specific guidelines. An appraiser may enter into an agreement to perform an assignment that calls for something less than, or different from, the work that would otherwise be required by the specific guidelines, provided that prior to entering into such an agreement: (1) the appraiser has determined that the appraisal or consulting process to be performed is not so limited that the resulting assignment would tend to mislead or confuse the client or the intended users of the report; (2) the appraiser has advised the client that the assignment calls for something less than, or different from, the work required by the specific guidelines and that the report will clearly identify and explain the departure(s); and the client has agreed that the performance of a limited appraisal or consulting service would be appropriate.

For the purposes of the Departure provision, the purpose and intended use of the appraisal or consulting service are critical. Intended users, other than the client, of the appraisal or consulting report might include parties such as lenders, employees of government agencies, partners of a client, and a client's attorney and accountant. From a liability standpoint, appraisers should be aware that unintended users of the report may come into legitimate possession of it through the normal course of business of the client. Clear and complete disclosure of all departures, what was and was not done and why it was or was not done, in appropriate sections of the report, will serve to prevent both intended and unintended users from relying on a report that may be unsuitable for other purposes.

### **How to Test a Departure**

A suggested test to determine if the appraisal would involve departure would be to ask the following questions: (1) Is there anything about the subject property or market I need to

acknowledge, but won't, in order to estimate value? and (2) Is there any analysis I should do, based on what reasonable appraisers would consider necessary for this engagement, but won't, in order to estimate value? If the answer to either of these questions is yes, the appraisal will probably involve departure. If an appraiser omits an approach to value or does not collect, verify, or analyze some data or condition because the appraiser does not believe it to be applicable or critical, and other reasonable appraisers and/or participants in the market for this type of property would not consider it to be applicable or critical, the appraisal will probably not involve departure. Elimination of an approach to value or some other analysis consideration constitutes departure only when that approach to value or that analysis consideration is applicable, critical, and is typically used for that type of property in developing a value estimate.

### **Types of Reports**

A report is any communication, written or oral, of an appraisal, review or consulting service that is transmitted to a client upon completion of an assignment. Each written report must be prepared under one of the following three options and prominently state which option is used. The essential difference among the three options is in the use and application of the terms *describe*, *summarize* and *state*. The client is responsible for selecting the appropriate type of report to support the purpose and intended use of the appraisal or consulting service.

Both the appraiser and the client should carefully consider the risk, size and complexity involved in the purpose and intended use and anticipated reliance on the report by third parties, intended and unintended, when determining the type of appraisal or consulting service and type of report format that will be required.

### **Self-Contained Reports**

A Self-Contained report is prepared under USPAP Standard 2-2(a) to document a Complete or Limited appraisal or consulting service. The Self-Contained Report is based on the word *describe* which is used to connote a comprehensive level of detail in the presentation of information. It contains, to the fullest extent possible and practicable, full and complete explanations of the data, reasoning, and analyses that were used to develop the opinion of value or the results of a consulting service. It also includes thorough descriptions of the subject property, the property's locale, the market for the property type, and the appraiser's opinion of highest and best use.

It should provide enough information on each topic so that a reader of the report can easily follow the reasoning without having to make leaps of faith. The reader should understand solely on the basis of what is written, how the appraiser arrived at his conclusion or recommendation. This is the recommended type of report for clients and intended users who have limited knowledge of the subject property and conditions that may affect its value and is commonly used in litigation.

### **Summary Reports**

A Summary report is prepared under USPAP Standard 2-2(b) to

document a Complete or Limited appraisal or consulting service. The Summary Report is based on the word summarize which is used to connote a more concise and less detailed presentation of information. It contains summary discussions of the data, reasoning, and analyses that were used to develop the opinion of value or the results of a consulting service. It also includes summary descriptions of the subject property, the property's locale, the market for the property type, and the appraiser's opinion of highest and best use. Any data, reasoning, and analyses not discussed in the Summary report must be retained in the appraiser's work file. A Summary report does not present full and complete details, it only presents the highlights of the information. A reader won't necessarily be able to follow exactly how the appraiser arrived at his conclusion or recommendation, but there should be no reason to doubt the appraiser either. This is probably the most common type of report given to clients. This is a sufficient type of report for intended users who have some level of knowledge of the subject property and conditions that may affect its value.

### **Restricted Reports**

A Restricted report is prepared under USPAP Standard 2-2(c) to document a Complete or Limited appraisal or consulting service. The Restricted Report is based on the word state which is used to connote the minimal presentation of information. It contains statements of the appraiser's findings with virtually no explanation of the data, reasoning, and analyses that were used to develop the opinion of value or results of a consulting service. All of the data, reasoning, and analyses in support of the appraiser's findings must be retained in the appraiser's work file.

There are no requirements for elaboration in a Restricted report, it basically only states the results. An exception to simply stating conclusions is that the extent of the process of collecting, confirming, and analyzing data must be described because the reader will have no clue as to what was done in order to arrive at the conclusion. This is the recommended type of report for a single client-intended user who has sufficient knowledge of the subject property and conditions that may affect its value. This type of report is also suited to situations involving client proprietary, sensitive, or confidential information when the purpose, function and intended use is solely for internal management purposes. This report should also contain a prominent use restriction stating that only the client is expected to receive or rely on it. This serves as a warning to any unintended users that the report cannot be understood properly without additional information in the workfile of the appraiser. □

### **AN ADDITIONAL LEVEL OF MEMBERSHIP?**

We have had mostly positive responses to Paul Fly's question about an additional level or class of members who do not meet all the criteria for Certification. Below follow several.

"I agree with the idea of alternate class memberships. It will

help growth and income of this fledgling organization."

*Ray Rathermel*

"This is in response to Paul Fly's proposal to create an intermediate level for those AIMA candidates who do not meet our criteria for Certification. I have been concerned for some time that we are losing some good candidates for certification simply because they lacked experience or training at the time of their application. The establishment on an intermediate membership level would, in my opinion, enhance AIMA's opportunity for growth. Therefore, I am supportive of Paul's proposal."

*Donald E. Warnkenen*

"A second class of membership, which might be considered, however, would be "Student Member" offered to graduates in mining engineering, mineral economics or geology, etc., who wish to pursue a career in mineral appraisal, or expend their expertise."

*J. Stuart Limb*

In view of this positive interest your Board will now prepare the groundwork for an associate member designation. In the meantime, please help us add a few members by selecting one of your peers as a candidate for membership in the AIMA. □

### **THINK ABOUT PROFESSIONAL DEVELOPMENT**

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I am attempting to write a textbook about the appraisal of solid minerals that is intended to have a content between the level of Betts and Ely's Basic Real Estate Appraisal and the Appraisal Institute's The Appraisal of Real Estate. I am looking for some people who would be willing to critically review chapters. No single source about minerals appraising is currently available and almost all of what is available is confined to a very narrow topic, deals with investment analysis as opposed to appraisal, or is essentially a company or government "handbook" for valuing a specialized interest of appraisal for a specialized purpose. I have yet to see one of them that actually tries to adapt the USPAP Standard Rules to a mineral property or mining company appraisal. Publishing the "book" has not been dealt with, "yet", but it may be advantageous for me and AIMA if we published it in a similar fashion to the way the Appraisal Institute does. I'd like to get some feedback on this idea.

*Editor's Note: I'd certainly volunteer to review a chapter. Any one else? AIMA could conceivably handle the publishing. This would be a good way for AIMA to get the name "out there".*

Another area for AIMA to look at is minerals appraisal issues involved in general litigation and takings. Most legal papers I have seen on these topics are addressed to lawyers and are either so esoteric as to be almost useless for an appraiser or so simple-minded that even a lawyer could understand it. Almost no one, especially the Uniform Standards for Federal Land Acquisition

seem to discuss the implications for mineral properties involved in Foster v. US or Whitney Benefits. Perhaps we could work with the Rocky Mountain and Eastern Mineral Law Foundations on a course suitable for appraisers and attorneys? Almost non-existent

discussion on other types of litigation involving mineral properties. We may be able to follow the lead of the ASA Business Valuation group in this area and develop and publish some specialized expertise.

*Editor's Note: Good idea! Who would volunteer to be our contact with the legal profession?*

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