

BEFORE THE BOARD OF REAL ESTATE APPRAISERS
STATE OF MONTANA

IN THE MATTER OF DOCKET NO. CC-07-0054-REA REGARDING:

THE PROPOSED DISCIPLINARY)	Case No. 799-2007
TREATMENT OF THE LICENSE OF)	
ANTHONY M. SMERKER,)	
Certified General Appraiser No. 251.)	
)	

**PROPOSED FINDINGS OF FACT; CONCLUSIONS OF LAW;
AND RECOMMENDED ORDER**

I. INTRODUCTION

The Montana Department of Labor and Industry Business Standards Division (BSD) filed a complaint against the appraiser's license of Anthony Smerker alleging violations of Montana Code Annotated § 37-54-403(1) (which requires a licensee to comply with the USPAP requirements)¹ and Montana Code Annotated § 37-1-316(18) (which prohibits a licensee from engaging in unprofessional conduct). Hearing Examiner Gregory L. Hanchett held a contested case hearing in this matter on January 31, 2007. Arthur Gorov, agency legal counsel, appeared on behalf of the Department of Labor and Industry. Smerker represented himself.

Smerker, a Montana certified general appraiser, and Billie VeerKamp, a Montana certified general appraiser and Board investigator, testified under oath in this matter. BSD's Exhibits 1 through 16 were admitted by stipulation of the parties. Based on the evidence adduced at the hearing as well as the arguments of counsel, the following findings of fact, conclusions of law, and recommended decision are made.

¹ "USPAP" stands for the Uniform Standards of Professional Appraisal Practice, the rules which regulate conduct of appraisers while conducting appraisals. These rules are promulgated by the Appraisal Standards Board of the Appraisal Foundation and govern the professional conduct of Montana appraisers by virtue of Mont. Code Ann. § 37-54-403. For purposes of the instant case, all references are to the 2005 Edition of USPAP which governs the appraisal at issue in this case.

II. FINDINGS OF FACT

1. At all times relevant to this proceeding, Smerker has held a Montana certified general appraiser's license.

2. Northern Trust Bank (bank) retained Smerker to complete an appraisal of a commercial retail and office development to be built on a commercial lot located in Big Sky, Montana. The bank sought the appraisal in order to determine whether to loan funds to the developer in order to build the development. Smerker accepted the assignment and ultimately completed two appraisals on the development. Both of these appraisals were subject to the requirements of the Uniform Standards of Professional Appraisal Practice (USPAP).²

3. The preliminary building footprint and building elevations (building plans) for the development were provided to Smerker in order to complete the appraisal (Exhibit 9). The building plans plainly show (even to the most uninformed observer) that the development was a commercial retail complex, consisting of two buildings. One building, the Aspen Building, was proposed to have 5 commercial suites (Exhibit 9, page 3). The other building, denominated as the "Hungry Moose Market Grocery and Deli" on the drawing elevation, contained only one suite (Exhibit 9, page 5). Smerker reviewed these plans prior to completing the appraisals at issue in this case.

4. The effective date of valuation of Smerker's first appraisal (Exhibit 6, Appraisal Report "B") of the property was January 7, 2005. The scope of the appraisal was to "estimate the most probable fair market value after the completion of the complex" (Exhibit 6, page 1). To complete this scope of work, USPAP standards applicable at the time required Smerker to complete all three methods of valuation of property, namely, the market (sales comparison) approach, the income approach, and the cost replacement approach. Without providing any analysis, Smerker invoked the Departure Rule and utilized only the cost approach. Under the applicable USPAP standards (the Departure Rule and Standards Rules 1-2(f) and 2-2(b)(ix)), he was not permitted to engage in such a departure.³ In order to produce a credible appraisal,

² The USPAP rules are promulgated by the Appraisal Standards Board of the Appraisal Foundation and govern the professional conduct of Montana appraisers by virtue of Mont. Code Ann. § 37-54-403. At hearing, BSD asserted that the 2004 edition of USPAP was applicable to this case. The date of the appraisal, as shown by both the complaint and the evidence at hearing, demonstrates that the appraisal occurred in January, 2005. The 2004 Edition of USPAP indicates effective dates of January 1, 2004 to December 31, 2004. The 2005 edition of USPAP indicates that it is effective as of January 1, 2005 and it appears to be applicable to this case. There is, however, no substantive effect upon this case in applying one or the other edition of USPAP since the language and numbering of the USPAP requirements at issue in this case is identical in both the 2004 and 2005 editions.

³ The USPAP applicable to this case contained the Departure rule which permitted variance from some USPAP requirements in certain circumstances when the rationale for the variance was adequately explained by the appraiser and the variance did not result in the creation of a report that was not credible. Effective July 1, 2006, the Appraisal Standards Board modified the USPAP standards to remove the Departure rule and implement the Scope of Work Rule. This change did not affect the appraiser's obligations in the development of values of opinion. See generally, Uniform Standards of Professional Appraisal Practice, *Revisions to USPAP and Advisory Opinions*, Page V (2006 Ed.).

Smerker was required to also address the market approach and the income approach. By failing to properly utilize all three approaches, Smerker created an appraisal that was not credible.

5. Smerker also failed to report reasonable exposure time of the property in his first appraisal. In addition, he failed to make necessary assumptions about the quality of the proposed construction. Smerker also failed to disclose the hypothetical conditions upon which his opinion of value was based. In addition, he failed to include an indication of the impact of the hypothetical conditions upon the value opinion.

6. Smerker's first appraisal also failed to adequately identify and report physical, functional and external market factors as they affected the appraisal. The appraisal itself identifies by a check box "increasing property values" but provides no corroboration for this assertion. Smerker did not include any information about competing commercial properties nor did he include any information about available vacant commercial sites in an effort to support his assertions.

7. Smerker's first appraisal also asserts that the highest and best use of the site was "commercial use." Once again, there is nothing in the appraisal to corroborate this assertion, such as information on competing properties, availability of sites, the demand for rental space in the local market, or anything mentioning leases in the local market. Furthermore, Smerker obviously did not consider the highest and best use of the property as improved in completing his appraisal. Smerker also failed to analyze economic demand and market area trends. While Smerker asserted that "the market in Big Sky, Montana is strong . . . with prices increasing," he provided absolutely no data to support that assertion.

8. The appraisal also suffers from a lack of appropriate valuation of the project site. Smerker's report identified only one **listing** as a comparable for arriving at the value of the site. The listing was not a closed sale as required by USPAP. Smerker's stated reason for not providing a closed sale for the comparable land was that "Montana is a non-disclosure state, and other sales are confidential." In fact, only county recorders are prohibited from disclosing information regarding closed sales. Information about closed sales is readily and lawfully available through local real estate sales persons and local listing services (see Exhibit 7, Standard 3 appraisal conducted on Appraisal B by Veerkamp, Numbered Paragraph 26).

9. Smerker's conclusions regarding the cost of the new improvements was also deficient. The report took all of the costs from the project developer without analyzing them against current market standards. There was no analysis or market information to support Smerker's statement that new construction has no depreciation. Furthermore, Smerker in essence equated the cost of building with the market value of the improvements to be built. As Veerkamp correctly noted in her review (and the hearing examiner finds), "the cost to build does not necessarily equal market value."

10. The bank obviously appreciated the lack of credibility that afflicted the first appraisal. This is evident because upon receiving the appraisal, the bank contacted Smerker and asked him to complete the appraisal again. One can surmise by reviewing Smerker's second appraisal (identified at hearing as Appraisal A and contained in Exhibit 4) that the bank

immediately recognized that the first appraisal was misleading because it was based solely on the cost approach to valuation. It appears that the bank asked Smerker to rectify this problem by furnishing an appraisal which contained an opinion of value based on all three methods of valuation - the income, market and cost approaches.

11. In conformity with the bank's request, Smerker developed a second appraisal containing opinions of income, market and cost values for the development. The effective date of this second appraisal (Exhibit 4, Appraisal Report "A") was also January 7, 2005. This second appraisal was substantially lacking in corroborating information and analysis. The report was riddled with USPAP violations. Not the least of these problems was that in developing the market approach, Smerker used individual residential condominiums as sales comparisons. As discussed in Finding of Fact 3, above, at the time of conducting the appraisal, Smerker had in his file and had reviewed the architectural drawings of the development. These drawings showed a site plan and building elevations that plainly demonstrated that two commercial buildings would be built on the site. The project has nothing to do with individual residential units. Yet Smerker inexplicably used individual residential condominium units as sales comparables.

12. In arriving at a valuation based on income, Smerker used the rents derived from residential properties instead of collecting and using information derived from commercial retail complexes. The rents derived from the residential properties which Smerker used as comparables have no relationship to rents derived from commercial properties. There simply is no professionally or logically justifiable basis for utilizing rents derived from residential units to develop an income based opinion of value for the development.

13. The USPAP deficiencies contained in Appraisal Report A rendered that appraisal not credible.

14. Smerker has been an independent fee appraiser for 15 years. By his own account, he has appraised both residential and commercial real estate, although it appears that the bulk of his commercial experience has been with farms and ranches. At hearing, BSD did not produce any evidence of any prior sanctions being imposed against Smerker's license.

15. Notwithstanding the lack of evidence of prior sanctions, the severity of the deficiencies in this case demonstrate an utter lack of competence in rendering commercial appraisals. With respect to the first appraisal, a minimally competent general appraiser would have known that in order to present a credible opinion of value under circumstances of this case (for purposes of mortgage lending), the scope of work would require all three valuation approaches (income, cost replacement and sales comparison) to be undertaken. Moreover, a minimally competent general appraiser would not have used individual residential condominiums as sales comparables for a commercial retail project as Smerker did in the second appraisal.

16. Smerker's lack of competence in completing commercial appraisals is reinforced in his suggestion at the hearing that he thought the project he was appraising was a residential project. It is doubtful that even a lay person could have made such a mistake when looking at

the architectural drawings (Exhibit 9) which Smerker had and had reviewed before undertaking the appraisals. Certainly, a minimally competent professional could not have made such a mistake. Sadly, his testimony that he thought the project was residential shows the depth of his lack of understanding of the opinion of value problem which he undertook in these two appraisals.

17. The BSD has sought revocation of Smerker's license as a result of his conduct in this case. The protection of the public in this matter requires that Smerker not be allowed to undertake commercial appraisals of any type until such time as he can demonstrate a least minimal competence in completing such appraisals. And, while there is no evidence of specific incidences of problems with Smerker's residential appraisals, his serious errors in developing the market approach to valuation in this case (most notably his inability to choose even remotely relevant comparables) call into question his ability to competently engage in appraisals of even non-income producing residential properties. This is because the most heavily relied upon approach to valuing non-income producing residential properties is the market value approach.

III. CONCLUSIONS OF LAW

1. The Board of Real Estate Appraisers has jurisdiction over this matter. Mont. Code Ann. § 37-54-105.

2. The Department bears the burden of proof to show by a preponderance of the evidence that the licensee committed an act of unprofessional conduct. Mont. Code Ann. § 37-3-311; *Ulrich v. State ex rel. Board of Funeral Service*, 1998 MT 196, 289 Mont. 407, 961 P.2d 126. The Department must also show that any sanction which it seeks is appropriate under the circumstances of the case.

3. Montana licensed appraisers must "comply with generally accepted standards of professional appraisal practice" as evidenced by USPAP. Mont. Code Ann. § 39-54-403(1). In addition, Admin. R. Mont. 24.207.402 provides that the Board adopts by reference USPAP standards.

4. The USPAP Ethics Rule, Conduct section, requires an appraiser to perform assignments ethically and competently, in accordance with USPAP. The rule specifically forbids an appraiser from communicating assignment results in a misleading manner.

5. The USPAP Competency Rule provides that prior to accepting an agreement, an appraiser must properly identify the problem to be addressed and have the knowledge and experience to complete the assignment competently or must disclose the appraiser's lack of knowledge to the client and then take all steps necessary to complete the assignment competently.

6. USPAP Standard Rule 1 requires an appraiser in developing an appraisal to "identify the problem to be solved and the scope of work necessary to solve the problem, and correctly complete research and analysis necessary to produce a credible appraisal."

7. USPAP Standards Rule 1-2(f) requires an appraiser to identify the scope of work necessary to complete the assignment. USPAP Rule 1-3(b) requires an appraiser who is developing a market value opinion to develop an opinion of the highest and best use of the real estate. USPAP Standards Rule 1-4(a) requires an appraiser who is developing a market value opinion to analyze such comparable sales data as are available to indicate a value conclusion. USPAP Standard 1-4(c) requires that where the income approach is applicable, an appraiser must, among other things, analyze either available comparable rental data or the potential earnings capacity of the subject property to estimate gross income potential of the property. USPAP Standards Rule 1-5 requires an appraiser who is developing a market value opinion to analyze all sales of the subject property during the three years preceding the effective date of the appraisal if such information is available to the appraiser in the normal course of business.

8. USPAP Standards Rule 2-1(c) requires a licensee to clearly and accurately disclose all assumptions, hypothetical conditions, and limiting conditions used in an assignment. USPAP Standards Rule 2-2(b)(ix) requires that an appraisal report summarize the information analyzed, the appraisal procedures followed, and the reasoning that supports the analysis opinions and conclusions contained in the reports.

9. Smerker's first appraisal violated the USPAP Competency Rule and Standard 1 by not correctly identifying the problem to be solved, the scope of work needed to solve the problem and by failing to correctly complete the research necessary to produce a credible appraisal. The appraisal developed and reported only the cost approach for a commercial project when the market and income approach were also required.

10. Smerker's first appraisal violated the Competency Rule and Standards Rule 1-2(f) by not identifying the appropriate scope of work necessary to produce a credible report. The first appraisal also violated these rules by failing to analyze the minimum amount of data needed to arrive at a credible value opinion for a proposed commercial complex.

11. Smerker's first appraisal violated Standards Rule 1-3(b) by not developing and reporting the highest and best use of the subject site.

12. Smerker's first appraisal violated Standards Rule 1-4(b)(I) by not developing an opinion of site value by an appropriate appraisal method or technique. Smerker's first appraisal violated Standards Rule 1-4(b)(ii) and Standards Rule 2-2(b)(ix) by using only cost data and fees provided by the developer and not at least verifying that information by comparing it to similar cost data in the market (such as cost data from similar commercial retail projects).

13. In several areas, Smerker's second appraisal violated USPAP Ethics Rule by failing to communicate an appraisal that was meaningful and not misleading. Not the least of the problems was the fact that the report used residential sales to derive a market value for a commercial retail complex.

14. Smerker's second appraisal violated the Competency Rule, Standards Rules 1-4(c) and 2-2(b)(ix) by failing to correctly verify, analyze and reconcile comparable data regarding rents for the commercial project in arriving at an income valuation for the subject

property. Smerker used rents from residential condominiums, a wholly inappropriate source for determining the income value of a commercial retail complex.

15. Smerker's second appraisal violated Standards Rule 2-1(c) by failing to clearly disclose the hypothetical condition upon which this appraisal rested, namely, that the improvements to the subject site were treated as though built on the effective date of the appraisal. Smerker failed to disclose this hypothetical and did not indicate what impact this hypothetical would have on the value conclusions that he reported in his second appraisal.

16. Smerker's second appraisal violated Standards Rule 1-(5) by failing to analyze sales of the subject property that had occurred within the three years preceding the appraisal.

17. Smerker's second appraisal violated Standards Rule 1-4(b) and 2-2b(ix) by not summarizing the information analyzed, the appraisal procedures followed and the reasoning that supports the analysis or the opinions of his cost approach valuation.

18. By failing to comport with USPAP requirements, Smerker committed unprofessional conduct. Mont. Code Ann. § 37-1-316(18) and Mont. Code Ann. § 37-54-403(1).

19. A regulatory board may impose any sanction provided for by Montana Code Annotated Title 37, Chapter 1, upon a finding of unprofessional conduct. Mont. Code Ann. § 37-1-307(f). Among other things, a regulatory board may revoke or restrict a license, may impose probation, may require remedial education, and may require monitoring of the practice by a supervisor approved by the regulating authority. Mont. Code Ann. § 37-1-312.

20. To determine which sanctions are appropriate, a regulatory board must first consider the sanctions necessary to protect the public. Only after this determination has been made can a board then consider and include in the order requirements designed to rehabilitate the licensee. Mont. Code Ann. § 37-1-312(2).

21. The depth of the errors committed by the licensee in this case (most notably the utilization of a "comparable" that even a lay person would find to be inappropriate) convinces the hearing examiner that adequate protection for the public requires that Smerker not be allowed to conduct appraisals for any commercial property. This would include retail complexes, farm and/or ranch property being valued as commercial property, or residential income property. He simply hasn't the competence at this time to be permitted to engage in such appraisals.

22. The hearing examiner also considered the possibility of recommending that Smerker be permitted to have a highly monitored practice under a restricted license which permits him to only complete appraisals of non-income producing residential properties. The genesis of this thought is the lack of any evidence at hearing showing that Smerker's license had been previously sanctioned or that he has had any problems in rendering appraisals of non-income producing properties. While at first glance this possible disposition has some appeal, further reflection convinces the hearing examiner that it is not a viable option. As noted in Finding of Fact Paragraph 18, above, Smerker's market approach to valuation of the

development was professionally and logically indefensible. Unlike commercial properties, appraisals of non-income producing residential properties very often rely primarily upon opinions of value derived from the market approach to valuation. Without some assurance that Smerker can competently select appropriate sales comparables to ensure the credibility of his market approach valuations, there is no way to ensure the public's protection even under a restricted license. The hearing examiner must conclude on the basis of the facts before him in this case that nothing short of revocation can protect the public while at the same time permitting Mr. Smerker to engage in the practice of appraising.

IV. RECOMMENDED ORDER

Based on the foregoing, the hearing examiner recommends that the Board of Real Estate Appraisers enter its order revoking the license of Anthony J. Smerker until such time as he can demonstrate to the satisfaction of the Board that he is minimally competent to safely engage in professional appraisal practice.

DATED this 20th day of March, 2007.

DEPARTMENT OF LABOR & INDUSTRY
HEARINGS BUREAU

By: /s/ GREGORY L. HANCHETT
GREGORY L. HANCHETT
Hearing Examiner

NOTICE

Mont. Code Ann. § 2-4-621 provides that the proposed order in this matter, being adverse to the licensee, may not be made final by the regulatory board until this proposed order is served upon each of the parties and the party adversely affected by the proposed order is given an opportunity to file exceptions and present briefs and oral argument to the regulatory board.