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Response #1130483

From Chris Thorne - Valuology

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Status Complete

1

Draft

UK VPS 3 Regulated purpose valuations: supplementary governance requirements

The requirements below are supplementary to Red Book Global Standards PS 2 section 5 – Disclosures where the public has an interest or upon which third parties may rely, and apply to Regulated Purpose valuations, namely:

- **valuations for financial reporting under UK VPGA 1 and UK VPGA 2 where these are relied upon by third parties**
- **valuations of local authority assets for accounting purposes under UK VPGA 4 but only in respect of investment property valued at fair value using IFRS 13**
- **valuation reports for inclusion in prospectuses and circulars to be issued by UK companies under UK VPGA 2.1**
- **valuations in connection with takeovers and mergers under UK VPGA 2.2**
- **valuations for collective investment schemes under UK VPGA 2.3 and**
- **valuations for unregulated property unit trusts under UK VPGA 2.4.**

Each one is a 'Regulated Purpose' and together 'Regulated Purposes'.

Valuers should refer to the exceptions at VPS 1-5 under PS 1 section 5. For example,

including but not limited to 'valuations for internal purposes only' is one that is not (or should not be) communicated to, and thus not entitled to be relied upon, by a third party.

The Regulated Purposes apply to all asset classes, including but not limited to specialist classes, for example, affordable housing and rural assets. However, the standards within this section only apply to valuation of those assets for a Regulated Purpose and those that are not subject to any applicable exceptions at VPS 1-5 under PS 1 section 5.

The Regulated Purposes apply to all types of asset holding arrangements including, but not limited to: limited partnerships, LTAFS, open and closed ended funds, other investment trusts, public pensions funds, REITS, UCITS funds, non UCITS funds (covered by AIFMD) and any other fund, trust or collective investment scheme regulated by the Financial Conduct Authority (FCA). However, the standards within this section only apply to valuation of those assets for a Regulated Purpose and those that are not subject to any applicable exceptions at VPS 1-5 under PS 1 section 5. For example, private funds, trusts and investments are only subject to the requirements where any related valuation would need to be relied upon by a third party and was not purely for internal purposes as defined at VPS 1-5 under PS 1 section 5.

The Regulated Purposes above do not include valuations exclusively for secured lending for which there is advisory content in VPGA 2, UK VPGA 10 (commercial secured lending) and UK VPGA 11 (residential mortgage).

Do you agree with the revised UKVPS 3 scope and definition as above?

No

Please enter any additional comments. Please provide objective justification and sufficient evidence to support your response.

The proposed introduction of mandatory rotation makes the definition of what types of valuation are subject to this change far more important than at present. "Valuations for financial reporting" potentially covers a very wide range of valuations for different purposes, asset types and businesses. For all apart from the smallest closed companies there will always be third party shareholders who may rely on valuations. The additional words proposed therefore effectively exclude no situation where a member is likely to be called upon to provide independent valuation advice to assist a client prepare financial statements. This will include valuations of owner occupied property, plant and

equipment, where the client has the option not to use the valuations in their financial reports anyway. There will be many situations when valuer has no knowledge of whether a third party will rely on the value provided or not. This extra condition does not limit the scope of what is regarded as a Regulated Purpose in any useful way.
Valuation advice may be required for purpose other than determining the carrying amount in the balance sheet of a major asset owned by a business entity, for example, to help the entity determine whether any asset is impaired and, if so, how it should be depreciated. Shareholders may be able to see what the entity has done as a result of the valuation inputs recieved but they are not relying on valuation advice itself. Further, such valuation advice is rarely sought on a recurring basis year after year but on ad hoc basis. When sought it will usually be from a valuer familiar with the asset because they provide other advice such as rating, rent review or other services, thus meaning they can provide the required input to management quickly and economically. To oblige the valuer to either turn down providing advice on depreciation apportionments or impairment because they last did so three years previously puts the client to unnecessary cost for no benefit to anyone given that the client is under no obligation to take such advice or act on it if received.

2

Do you have any suggested changes to the revised scope and definition?

Please provide objective justification and sufficient evidence to support your response.

The focus of the Pereira -Gray review was purely on Investment Property held in investment funds or companies. Under IFRS and other accounting standards these ARE required to be individually valued at each reporting date. To avoid overreaching the purpose and target of the Pereira-Gray review and causing unintended consequences

for other types of valuation inputs into financial reporting generally, we believe the proposed additional words to valuations for financial reporting “where these are relied upon by third parties.” should be deleted and replaced with “of Investment Property under IAS 40 or UK FRS 102 Section 16.”
A similar condition is already proposed to restrict the Regulated Purpose requirement for public sector financial reporting to valuations of investment property. It follows that we support this.

3

What additions or exclusions would you make to the revised scope and definition?

Please provide objective justification and sufficient evidence to support your response.

see above

4

What is your view on the cost of implementation and business impact (whether positive or negative) of the revised UK VPS 3 definition, and the benefits?

Please provide objective justification and sufficient evidence to support your response.

Including any type of valuation advice provided for finacial reporting purposes within the scope of Regulated Purpose valuations and the rotation policies will have a negative impact on clients when they are neither required by the relevant accounting standards nor any other applicable regulation to have assets valued on a regularly recurring basis. This is because entities could not simply seek advice from the same firm that has advised them on their property, plant and equipment holdings for many years, which will increase the cost of obtaining the advice they require with no corresponding benefit to their shareholders.

5

Draft

UK VPS 3.3 Rotation

Explanatory note on UK VPS 3.3 covering rotation and transition

The intention of the changes suggested to UK VPS 3.3 is to introduce a mandatory rotation policy so that the continuous relationship between a client and a valuer and/or firm providing valuations for the same regulated purpose in the UK will not exceed eight years. The proposals aim to ensure public trust in the reliability of valuation and prevent conflicts of interests, which may arise between long term valuation advisers and clients. Relationships between clients and valuation advisors for other non-regulated purposes are not affected by the proposed changes.

RICS recognises that tendering for a new valuation advisor can take some time. The proposed transition policy seeks to provide a reasonable timescale to allow clients to make an orderly transition to a new valuation advisor, where their existing contracts are due to end within three years of the introduction of the rotation policy, by allowing these contracts to be extended by eighteen months. RICS considers that this policy allows firms and clients to act in order to spread the necessary changes of valuation advisors over a five year period effective from the publication of the policy, reducing the risk of disruption in the market.

There will also be contracts that were put in place before the introduction of this policy which provide for continuing relationships of more than eight years and will therefore need to be brought to an end where it is lawful to do so. The transition policy proposed would require firms to end such contracts no later than three years from the implementation of the changes, where they can do so lawfully and without an unreasonable penalty. What is unreasonable will be a question of fact in the particular circumstances. This again provides an opportunity for firms and clients to either enter into new contracts which comply with the new rotation policy where possible, or to use this three-year period to transition to new valuation advisors where that is required.

UK VPS 3.3 Rotation

Where a valuation is to be undertaken for a Regulated Purpose, the valuer must confirm in writing that a rotation policy is in place at their firm. In order to undertake the valuation, the valuer must be able to confirm to the client in agreed written terms of engagement (as an addition to VPS 1) that the period for which the client has procured UK valuation services from the valuer and or valuer's firm for the same Regulated Purpose (the continual contractual relationship) does not exceed five years, and will not have exceeded it by the end of the new instruction. This is save for cases where there has been a break from valuation instructions for the same client for at least five consecutive years, or where at the fifth year or earlier a service review, which is defined below, has occurred, or where the transitional provisions below apply.

A service review must be undertaken by an external third party acting for the client such as an auditor or one of the following independent internal roles, (or a role of equivalent power and/or authority):

a. a non-executive director

b. an independent chair of the firm's audit committee

c. a corporate compliance officer.

A service review allows the potential for an extension of valuation services by the firm (but not the same valuer) for up to a further three years, where the external reviewer or independent internal reviewer certifies in writing that there are no conflicts of interest or other matters that might materially impact the quality, accuracy or efficacy of valuation services. Only one service review is allowed prior to any five-year break period. A contract may only be extended following a service review where the continual contractual relationship at the end of the extension will not exceed eight years.

Do you agree with the proposed UKVPS 3.3 covering rotation?

Somewhat/Partially

Please enter any additional comments. Please provide objective justification and sufficient evidence to support your response.

We agree only if the scope is confined to the target of the PP-G Review, i.e. investment property held in regulated funds, Real Estate Investment Trusts, or for any other entities with material holdings of investment property. Applying manadatory rotation for every valuation that may assist a client in determining how any type of asset, or liability, should be accounted for in their financial statements will only add delay and cost to the client for no identifiable public benefit.

6

Do you have any suggested changes to the proposed UK VPS 3.3?

Please provide objective justification and sufficient evidence to support your responses to the questions.

If the problem identified above is solved by narrowing the scope of what is a "Regulated Purpose" valuation, no.

7

Are there areas where more flexibility should be built into the mandatory rotation policy?

Please provide objective justification and sufficient evidence to support your response.

We cannot identify any provided it applies only to recurring valuations for entities with material holdings of investment property.

8

Please set out any additional wording or exclusions you would make to the proposed UK VPS 3.3?

Please provide objective justification and sufficient evidence to support your response.

n/a

9

What is your view on the cost of implementation and business impact (whether positive or negative) of the new UK VPS 3.3, and the benefits?

Please provide objective justification and sufficient evidence to support your response.

The potential negative affects on client's unless the scope of "Regulated Purpose" valuations is limited to the subject of the Pereira-Gray review has already been addressed in our repsonse to question 1.

10

Draft

Transition to valuer and firm rotation

The dates included in the following section are subject to the approval of the RICS Standards and Regulation Board and may be subject to change.

- From 1 October 2023 the valuer and firm rotation arrangements set out in UK VPS 3.3 become mandatory: It prescribes a maximum five-year continual contractual relationship period for valuation services for a Regulated Purpose, with the option of up to a three-year extension period, subject to a successful service review. This is followed by a mandatory break of five consecutive years until the next permitted instruction of that valuer and/or firm.
- A regulated valuer and/or firm considering entering into a new contract or continuance of an existing contract for valuation services in respect of a Regulated Purpose on or after 1 October 2023, must take into account any pre-existing contractual relationship had by the valuer and/or valuer’s firm with the client prior to 1 October 2023, in assessing their compliance with the new rules under UK VPS 3.3.
- Subject to the terms of the transitional provisions detailed below, valuers and/or firms

may complete existing contracts with clients that are ongoing on 1 October 2023.

- Where a valuer and/or valuer's firm as at 1 October 2023 is engaged in an existing valuation contract for a Regulated Purpose and that contract either may or must be brought to an end on or before 30 September 2026, the valuer and/or valuer's firm may extend the contract for one period not exceeding 18 months, without a service review having occurred, even where the continuing contractual relationship exceeds or will exceed eight years, without breaching the rotation policy, in order to allow an orderly rotation to a new valuation advisor.
- Where a valuer and/or valuer's firm as at 1 October 2023 is engaged in an existing valuation contract for a Regulated Purpose which ends on or after 1 October 2026 **and** the continuing contractual relationship will have existed for a duration of eight years or more at the contract end date, valuers and/or valuer's firms must ensure that the new rotation policy stated in UK VPS 3.3 is applied by ending or varying the contractual relationship no later than 1 October 2026 to ensure that the continuing contractual relationship does not exceed five years, where they can do so within the terms of the contract (for example a valuer's without penalty break provision; or the exercise of a right to terminate on reasonable notice; or termination by agreement (this is not an exhaustive list)) and without unreasonable penalty.

Do you agree with the proposed rotation transition policy as above?

Yes

Please enter any additional comments. Please provide objective justification and sufficient evidence to support your response.

Subject to the scope of valuations to which manadatory rotation applies being limited to recurring valuations of investment property, we agree.

11

Do you have any suggested changes to the proposed rotation transition policy?

Please provide objective justification and sufficient evidence to support your response.

No

12

What additions or exclusions would you make to the proposed rotation transition policy?

Please provide objective justification and sufficient evidence to support your response.

n/a

13

What is your view on the cost of implementation and business impact (whether positive or negative) of the proposed rotation transition policy, and the benefits?

Please provide objective justification and sufficient evidence to support your response.

see previous comments

14

Draft

UK VPS 3.4 Terms of engagement and instructions

In addition to the standards set out in Red Book Global Standards VPS 1, the valuer must verify that the instruction or draft instruction has been made with the approval of one of the following authorities from the client (or a role of equivalent power and/or authority):

a. a non-executive director

b. an independent chair of their audit committee or equivalent

c. a corporate compliance officer or equivalent.

This should be explicitly and expressly detailed within the final instructions and terms of engagement and clearly stated within the valuation report, including within any published version.

The valuer should also confirm with the client in agreed written terms of engagement whether any of the instructing client parties receive a direct fee or benefit as a result of the valuation, including, where relevant, its comparison to performance indices or other benchmarks. Where this is the case, it must be clearly stated within the terms of engagement and report, including any published version.

Where any instructing party, including in respect of draft instructions, is an RICS member, the valuer should highlight to the member their obligations under RICS' Rules of Conduct and the current edition of RICS' Conflicts of Interest. Confirmation that this has been undertaken should be included within the valuation report, including any published version.

Permission for the valuer and their firm to use client data from the valuation for other valuation and business activities must either be expressly confirmed within the written term of engagement, otherwise there should be a written statement confirming such data will not be used for other valuation or business activities. The valuer must ensure that adequate data security is in place to safeguard inadvertent or inappropriate sharing of such data, internally or externally. Valuers are reminded of the confidentiality requirements contained in PS 2 section 3 of Red Book Global Standards.

Do you agree with the proposed UK VPS 3.4 as above?

No

Please enter any additional comments. Please provide objective justification and sufficient evidence to support your response.

This proposal expects the RICS Valuer to be able to determine the policies and procedures adopted by their clients. This is unrealistic and unreasonable. Absent any law or regulation that requires clients to seek specific approvals before commissioning valuations or for fund managers to disclose their fee basis, RICS in is no position to force compliance on third parties nor to expect its members to do so. Neither is it reasonable to expect members to tell a client who happens to be an RICS member of their obligations under the Rules of Conduct. It is for RICS to regulate its members, not to expect members to regulate any client who is also a member.

If the RICS considers that such procedures would be in the public interest they should be lobbying the competent authority (the FCA) to introduce regulations. It is extremely presumptuous for RICS to assume it can dictate how funds and other investment entities are managed.

15

Do you have any suggested changes to the proposed UK VPS 3.4?

Please provide objective justification and sufficient evidence to support your response.

It should be deleted for the reasons explained above.

16

What additions or exclusions would you make to the proposed UK VPS 3.4?

Please provide objective justification and sufficient evidence to support your response.

It should be deleted

17

What is your view on the cost of implementation and business impact (whether positive or negative) of the proposed UK VPS 3.4, and the benefits?

Please provide objective justification and sufficient evidence to support your response.

n/a

18

Draft

UK VPS 3.5 Preliminary advice, draft reporting, and client discussions

Valuers should be familiar with Red Book Global Standards PS 2 paragraphs 3.12-3.15 covering preliminary advice, draft reporting, and valuation discussions.

The requirements of PS 2 paragraphs 3.14 and 3.15 are amended for UK Regulated Purpose valuations as follows, and are therefore mandatory.

To demonstrate that valuation discussions have not compromised the member's independence, a file note of discussions with the client on draft reports or valuations must include:

- the information provided, or the suggestions made, in relation to the valuation
- how that information was used to consider a change in material matters or opinions, and
- the reasons why the valuation has or has not been changed.

A file note can be digital or based on a transcript of recorded meetings but must be capable of being produced for appropriate third parties where so needed. The file note should be countersigned by a: non-executive director, independent chair of their audit committee, a corporate compliance officer or a role of equivalent power and/or authority, confirming that they have overseen the resulting changes.

If requested, this record must be made available to auditors or any other party with a legitimate and material interest in the valuation.

When providing a valuation as part of a tendering process, valuers are reminded that Red Book Global Standards and those of this UK national supplement apply. In such circumstances valuers should be mindful of the need to provide objective and accurate valuation advice and should not be swayed by the opportunity to win new business.

Do you agree with the proposed UK VPS 3.5?

No

Please enter any additional comments. Please provide objective justification and sufficient evidence to support your response.

It is unclear who should countersign the file note. The reference to "non-executive director", "chair of the audit committee" or "corporate compliance officer" implies that these are not roles within the RICS Regulated firm (few of which have such roles) but representatives of the client.

If it is intended that a client representative should sign the valuer's record this is another example of overreach by RICS. It cannot oblige anyone other than its members or their firms to comply with the Red Book, or any other RICS rule. While it might be considered good practice to obtain a client's acknowledgement of a record of discussions about draft valuations, neither the valuer nor RICS are in a position to enforce this if the client fails to sign.

19

Do you have any suggested changes to the proposed UK VPS 3.5?

Please provide objective justification and sufficient evidence to support your response.

The requirement to obtained the client's signature needs to be changed to a recommendation given that neither the member nor RICS is in a postion to enforce compliance.

20

What additions or exclusions would you make to the proposed UK VPS 3.5?

Please provide objective justification and sufficient evidence to support your response.

see above

21

What is your view on the cost of implementation and business impact (whether positive or negative) of the proposed UK VPS 3.5, and the benefits?

Please provide objective justification and sufficient evidence to support your response.

see above

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Response #1131528

From Chris Thorne - Valuology

Date Started: 12 Dec 2022 13:10. Last modified: 13 Dec 2022 11:59

Status Complete

1

Do you have any comments on the updates to the financial reporting sections (UK VPGAs 1-3, 8 and 9)?

Please provide objective justification and sufficient evidence to support your response.

As an interim step we agree with the proposed changes. However, the lack of guidance on IFRS requirements in the Global Red book has to be addressed, and this may in turn lead to revisions in the UK Supplement in the future. However, it may be more appropriate to consider issuing guidance on financial reporting valuation requirements as "Professional Information" in the future, given that the relevant standards are not set by RICS.

2

Do you have any comments on the updates to the public sector sections (UK VPGAs 4-6, 16 and 17)?

Please provide objective justification and sufficient evidence to support your response.

We think the changes to UK VPGAs 4-6 should help prevent some inappropriate interpretations of what the relevant accounting standards require.

The professional standard and guidance for CPO and compensation should be in one place. It is to be hoped that the contents of UK VPGA 16 can be merged into the revised PS on Compulsory Purchase and Compensation and removed from the Red Book.

3

Do you have any comments regarding the updates to the Residential valuation section (UK VPA 11)?

Please provide objective justification and sufficient evidence to support your response.

The rationalisation and avoiding duplication of material that is covered in standalone guidance or other Professional Standards is welcome.
One material change we are concerned about is the proposed new material on dealing with requests for valuations assuming a restricted marketing period or "forced sales".
The existing guidance that says the valuer should use a “Projected Market Value” when asked to advise on value for possible possession proceedings is clearly flawed, both conceptually and in terms of its suitability. We therefore welcome the proposal that this be removed.
The proposed new UK VPGA 10.11 on restricted marketing periods draws attention to VPS 4, specifically that providing such advice without a clear reason for the restriction is contrary to the standards. If a client insists on such advice it says that the valuer should a) point out in their terms of engagement that is not in accordance with the RICS standards and, b) refer to the limitations on this figure and the risks of relying on in the report. However, it goes on to include a proposed definition for use when a client asks for a value in a “forced sale”. We have no problem with providing such a definition in principle but do with the way this is presented and with the definition provided.

While paragraph 6 of 10.11 does refer to “the principles set out above” and the commentary in VPS 4 (presumably the specific reference to restricted marketing periods), the fact that it is detached from the principles in question by a subheading means that it is easy to miss the important conditions on providing such advice.

As regards the wording of the definition, we believe it is a mistake to refer to the time limit being to legal completion. The time it will take to complete legal formalities, whether it be exchange of contracts or completion, depends on matters which are not only outside the valuer’s knowledge and professional expertise but which can also have little effect on the price that can be obtained. The RICS should not be encouraging members to provide such a hostage to fortune. The time limit should for reaching agreement, subject to contract.

4

Do you have any comments on other sections of the UK Supplement to the Red Book not specifically updated and consulted on here?

Please provide objective justification and sufficient evidence to support your response.

No

5

Do you have any comments on the UK Supplement to the Red Book as a whole?

Please provide objective justification and sufficient evidence to support your response.

Some of the VPGAs duplicate subjects also dealt with in standalone Guidance Notes. Now that RICS has decided there should just be two categories of standards document, "Professional Standards" and "Practice Information", it is to be hoped that most of the current VPGAs and standalone Guidance Notes on valuation matters can be consolidated into Practice Information, and the Red Book and its supplements simplified as a result.

6

Do you have any comments on the wording of any section of this draft UK National Supplement?

If so, please specify the section number/title/paragraph in the document and what wording you would change or what your comment on the wording is.

Please provide objective justification and sufficient evidence to support your response.

see comments on proposed UK VPGA 10.11 in answer 3.

7

Please provide your email address if you are happy for us to contact you for further information and/or to keep you informed of updates.

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