RICS Valuation – Global Standards - What has changed?

At the end of November RICS issued a revised edition of the Global Red Book. This supersedes the RICS Valuation – Global Standards 2017 and therefore becomes the authoritative set of standards for all RICS Valuers. The new standards become effective from Friday 31 January 2020. We review the new edition and offer our comments and observations on the implications of the changes for RICS valuers.

Download the new Global Red Book

Download the "Basis for Conclusions"

Overview

The good news is that the changes to the RICS standards proper are relatively few in number and valuers who are currently complying with the 2017 edition are not going to need to make any material changes in what they do. However, some complications may arise from changes to the IVS, which, as previously, are bundled together with the RICS standards. The IVS are not included in the Red Book simply for information. As is stated in the Introduction, the PSs are mandatory and "define the parameters for compliance with the Red Book Global, including adoption of the International Valuation Standards".

Since most RICS valuers are real estate specialists, the main area of concern arising from the IVS changes is in relation to the valuation of development property for secured lending. The following provision has been introduced into IVS 410[1]:

> *"To demonstrate an appreciation of the risks involved in valuing development property for secured lending or other purposes, the valuer should apply a minimum of two appropriate and recognised methods to valuing development property for each valuation project…"*

RICS has never before attempted to direct how its members should value a given type of property in given circumstances, having previously recognised that this is both impractical and contrary to the ethos that it is the valuer's professional responsibility to choose the appropriate method or methods to adopt. However, this direction is now embedded in the Red Book via the back door of the IVS. In conversation with RICS staff we have been told that because the word "*should*" is used they regard this as advisory and therefore the valuer still has discretion. This overlooks the fact that the IVS now define "*should*" as being "presumptively mandatory", meaning the valuer must comply unless they can demonstrate that alternative action was sufficient to comply with the objective of the standards.

There will be many occasions when the use of more than one method to value development property is inappropriate, impractical or both. Even though RICS may internally regard the IVS requirement as merely advisory, if a member had to defend the use of a single method in a legal dispute, the words in the IVS could be problematic given the RICS's statements elsewhere that its Professional Standards adopt the IVS. It would be advisable for firms involved in development valuation to revisit their procedures and report wording to minimise the potential for problems arising from this ill-advised change in the IVS.

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[1] IVS 410 Development Property 120.2

Summary of Changes

Title:
The title of the current edition is "RICS Valuation – Global Standards 2017". It might be expected that the replacement would be "RICS Valuation – Global Standards 2020". Instead the new edition is "RICS Valuation – Global Standards" but with the effective date shown beneath this.

> **Comment:**
> RICS have not commented on this change but it appears it has followed the lead of the IVSC in not using the year of issue as an identifier. The reason given by the IVSC for its change was because it foresaw the need for more than one update within the same year, notwithstanding the fact that the usual interval between updates during the past twenty years had been at least two years. However, even if this does arise, RICS does not have to automatically follow suit. Given the regulatory status of its standards there is a strong argument that RICS needs to maintain certainty as to which rules apply to its members on any given date and that changes should be made on the basis of a clearly understood process and timetable.

Introduction: Paras 20 and 26 - Effective Date.
Para 20 confirms that the effective date of this edition of the Red Book is 31 January 2020 and states that it applies to all valuations where the valuation date is on or after that date. Para 26 confirms that the version of the IVSs included in Section 6 of the Red Book is also the version effective from that date.

> **Comment:**
> Although only the dates have changed from the previous edition, the question of effective dates needs a rethink. The date on which a member is required to comply with new pronouncements issued by RICS should be the date on which the service is provided, not the valuation date. Retrospective valuations are frequently required but it is surely desirable that these are undertaken under the most recent Professional Standards rather than those that applied at an earlier date. For example, recent editions of the Red Book have seen a progressive tightening of the requirements around the investigation and disclosure of potential conflicts of interest. If the later, more rigorous, requirements are deemed necessary for the better protection of clients' interests then they should apply regardless of the valuation date.
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> Additionally, the fact that IVSC has chosen to identify its most recent edition of the IVS by reference to a supposed effective date of 31 January is irrelevant to RICS. The IVSC is only a creator of standards; it has no powers to enforce their application, nor to stipulate an effective date. It is for those adopting the IVS by including them in professional or statutory regulations to determine when they will be effective within their jurisdiction.

PS1 1.3: Meaning of "written"
A new sentence has been added to confirm that the Red Book applies not only to a valuation provided in writing in the traditional sense. It applies to any valuation conveyed by paper, by any electronic or digital means or form of recorded media.

> **Comment:**
> While we are not aware of anyone believing or claiming that a report delivered using a medium other than conventional writing was not covered by the Red Book, this is a useful clarification.

PS2 1.5: The need for Professional Scepticism

The current requirement for members to be independent and objective in their approach to valuations is now reinforced by the requirement to apply professional scepticism to information and data relied on as evidence. This term comes from the world of audit and simply means that as an independent professional, a member must not just accept evidence, for example comparable transactions provided by third parties or cash flow forecasts provided by the client, without critical consideration and analysis. The revised PS2 1.5 describes professional scepticism as an "attitude that includes a questioning mind, critically assessing evidence relied on in the valuation process and being alert to conditions that may cause information provided to be misleading."

Comment:
This is a useful reminder that valuation is not simply a technical process calculating a figure based on various data inputs but one that requires professional judgement. In a world where the mathematical processes of valuation are increasingly automated, the value of the valuer is in proper scrutiny of the inputs into the calculation to ensure that these are relevant and reliable.

VPS1 3.2 (d): "Non-Financial Liabilities"

This is simply the addition of a cross reference to the recently issued IVS 220 on "Non-financial Liabilities" to the list of matters that need to be considered when identifying the asset or liability to be valued in the Terms of Engagement.

Comment:
While some members may be puzzled by the term "non-financial liability", which is not helped by IVS 220 having been written almost exclusively from a business valuation perspective, it can include liabilities that frequently have to be taken into account by real estate valuers such as environmental clean ups or repairing obligations. We did suggest that to be helpful to the majority of its members RICS should expand on this topic. In its "Basis for Conclusions" document RICS say that guidance on the practical implementation of IVS 220 will be considered for a future Red Book Global update.

VPS3 2.2 (l): Additional commentary on disclosure of valuation approach and reasoning

Two additional paragraphs have been added to the explanatory text (headed "Implementation") for the requirement to include the valuation approach and reasoning in the report unless it has been expressly agreed otherwise with the client.

The first of these paragraphs indicates that the explanation provided in the report should be "…proportionate to the task, being focussed on assisting understanding by the client and other intended users." In other words, in most cases members should avoid excessive technical detail or jargon and provide straightforward explanations which will be clear to the recipient of the report and any others who may rely on it. A further proviso is that if there has been any deviation from common practice in the profession this should be highlighted.

The second paragraph provides that, wherever appropriate, the relevance and significance of sustainability and environmental matters should form an integral part of the valuation approach and reasoning supporting the reported figure. The requirement to consider such matters is already included (see VPS2 1.5 and VPGA 8) so this addition is simply confirming that the impact of any findings on the valuation should be reflected in the reasoning in the report, wherever this is appropriate.

Comment:
These are useful additions. Of particular relevance are the words "proportionate to the task" and "wherever appropriate". We have seen a tendency for some members including "boilerplate text" in their reports purporting to provide information about the method and reasons for their valuation, in the belief that by doing so they are ticking the box in the Red Book that requires these matters to be disclosed. This can confuse or mislead the reader with either excessive technical detail or explanations which are of little or no relevance to either what is being valued or the purpose for which the valuation is required, which is itself contrary to the General Principle of VPS 3. This section of a report can rarely be successfully standardised.

VPS5 para 5: Inclusion of reference to "valuation modelling"

This paragraph is effectively a cross reference to IVS 105, where a small amendment has been made to include the responsibilities of valuers in relation to valuation modelling in the list of matters covered by the IVS Standard.

Comment:
This change is of little consequence. Section 90 "Valuation Model" has been added to IVS 105 and this requires the valuer to keep records of why the model was selected or created, to ensure it is consistent with the required basis of value and that the key risks of assumptions made in the model are considered. However, since IVS 102 also requires the valuer to keep a record of the key inputs, all calculations, investigations and analyses relevant to the final conclusion, matters also echoed in VPS2 of the Red Book, it is merely repetition of something valuers should have been doing anyway.

VPGA1 – Valuations for Inclusion in Financial Statements

A lengthy new section 5 has been added called "Performance Standards". However, this simply recites provisions that appear elsewhere in the Red Book relating to competence and professionalism, terms of engagement, sources of information, documentation and reports. It does not include any additional or specific requirements for a member undertaking a valuation for inclusion in financial statements.

Comment:
In its Basis for Conclusions, RICS indicate that this section was included to draw attention to a number of mandatory requirements in earlier parts of the Red Book and serve as a useful reminder or checklist. The same argument could be made for including such a section for valuations for any other purpose. All this repetition achieves is to make the Red Book longer than it needs be and therefore less accessible to members. It also unnecessarily complicates future updates by requiring any change to be reflected in multiple sections.

Since the IVSC has excluded from its last two editions any guidance on this subject, which is the one type of valuation that needs to be consistent across borders and which was the prime reason for the IVSC's creation, it might have been expected that RICS would seek to help its global membership by providing useful guidance on the main valuation requirements under IFRS instead of this pointless space filler.

VPGA 7 Antiques and Fine Arts
There are many detailed amendments to the previous VPGA but these can mainly be classified as clarification or explanation of how provisions in the rest of the Red Book apply. The only significant additional requirement is to require the valuer to undertake an appropriate level of due diligence in relation to establishing the provenance of the item to be valued.

> **Comment:**
> The changes made are consistent with the consultation draft. The Basis for Conclusions indicates that no objections were received, so it is presumed that the text was approved by the Antiques & Fine Arts Professional Group.

VPGA 8 Valuation of Real Property Interests; Guidance on Environmental Matters
A minor addition has been made to 2.6 (c) (ii) on sustainability to include "current and historic land use" to the list of matters that may be relevant to the value of property.

> **Comment:**
> While RICS correctly identify sustainability as a factor that influences decisions to buy or sell and therefore values, it is necessarily vague about what exactly a valuer has to do except be aware of the influence "sustainability factors" may have for a particular property type in a particular market. This change does not have any material impact on the valuer's responsibilities in this regard.

Conclusion

This new edition has clearly been driven by a perceived need to shadow the IVS by bringing out a new set of RICS standards with the same effective date. However, we disagree that this should be the main reason for a new edition of the Red Book, especially when this means that matters which are currently more significant for many RICS members have not been addressed in order to meet this supposed deadline. These include a possible update to the guidance on material valuation uncertainty and supporting material on the implications of the new IVS on "non-financial liabilities" for real estate valuers. Both of these are mentioned in the "Basis for Conclusions" as being considered for inclusion in a future edition, but when will this be?

With the IVSC announcing that it intends to increase the frequency of updates to the IVS we feel that it is time for RICS to review the process of how and when IVS updates are brought into RICS Practice Standards and to clarify the status of the IVS material when it is published alongside similar but slightly different pronouncements made by RICS within the same set of standards.

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