
Dear <<First Name>>
Marianne Tissier and Chris Thorne welcome you to our
latest Newsletter

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Valuology

We are pleased to bring you our thoughts on a few recent developments in the world of valuation. These range from the findings of a recent review into valuations for investment funds, through possible new challenges when preparing valuations for financial reporting to a few useful reminders for valuers to help keep them out of court.

Setting standards

We are pleased to announce that Chris has been appointed as a member of the new “Global Valuation Standards Expert Advisory Group” established by the RICS to advise on valuation standards. Following governance changes at RICS in 2020 there are now just three decision making boards. The Standards and Regulation Board (SRB) is the body that approves all new professional standards, including the Red Book. The GVSEWG has been established to advise the SRB on valuation standards. Chris is one of ten members drawn from around the world that make up the group, chaired by Nick French, who will be well known to many who trained at either Reading or Oxford Brookes Universities in the last thirty years. From its initial meeting it is clear that the group will have a full agenda, not least the role of the Red Book, its relationship with the IVS and reviewing the output of other specialist groups that impact on the valuation standards. As always, we will endeavour to keep you up to speed with developments, but one of Chris’s priorities is to improve member engagement in the development of the Red Book and the supporting guidance issued by RICS.

Investment valuation review

Those of you based in the UK probably will have seen publicity around the recent report and recommendations from Peter Pereira -Gray. This report was commissioned by the SRB into the valuations provided for real estate investment funds and companies following some high profile criticisms of RICS valuers in the financial pages of the press during 2019. While much of this criticism was misinformed and based on simplistic contrasts between the total share capital and the NAV of listed REITS, nearly 20 years had elapsed

since RICS last commissioned an external review into the sector by Sir Bryan Carsberg so a critical review was probably due. The SRB has announced that it has accepted all the recommendations made by Pereira-Gray, but RICS has a lot of work to do to implement many of these, including considering changes to the Red Book, CPD requirements and more specific guidance around avoiding conflicts of interest in valuation. To achieve other recommendations, it will need to engage with client side organisations and, in some cases, financial regulators as some of the required actions are not entirely within the control of RICS members.

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DCF - No need for concern?

Generally the recommendations in the Pereira-Gray Review have been well received by the large firms who are mainly involved in valuations for the institutional market, which was its primary focus. However, care will need to be taken to ensure that any changes RICS make do not have unintended consequences for the smaller firms who do not deal with this market. One obvious example is the recommendation that discounted cash flow should be the principal model applied to property investment valuation. This has already attracted criticism, mostly because it is being interpreted as recommending RICS should make the use of DCF a mandatory or quasi mandatory requirement for all investment property regardless of type or size. When read in the context of the whole report we do not believe that it was intended to recommend extension of the use of DCF models beyond the type of property for which it is already the most suitable method. We, therefore, consider it unlikely the Red Book is going to mandate the use of DCF anywhere or suggest it is appropriate in markets where market participants use other methods to establish prices. But watch this space.

Are you compliant?

One aspect of the Pereira-Gray Review which could have implications for many firms, whatever their size, is the recommendation that any firm undertaking valuations for a regulated purpose should have a Compliance Officer ("CO"). He expressly includes sole practitioners in his recommendation. The role of the CO would be to oversee compliance by the firm with all the applicable statutory, regulatory and RICS standards for the process and conduct of the valuation. The SRB has indicated that RICS will set about defining the requirements for this role, which is separate from that of the "Responsible Principal" under the RICS Firms Registration scheme, but it is not yet clear what that process will involve. While larger firms will be able to support a permanent CO, small to mid-size firms will hopefully be allowed an alternative means of fulfilling the role, such as appointing a consultant to advise as and when required. However, while we await the detail, the Review is a useful prompt for firms of all sizes to review their current valuation procedures, especially around matters such as avoiding conflicts and compliance with the specific standards and regulations affecting the work they do.

Explaining the numbers

Valuers instructed to provide a valuation for use in financial statements issued by their clients need to be aware of how it is to be presented in those statements. Where the statements are prepared under IFRS, the client will need to include some specific information, or “disclosures”, about the valuation, and valuers are sometimes asked to provide information to assist with these. The IASB has received feedback that current disclosures about many items in financial statements either provide not enough relevant information, too much irrelevant information or do not communicate information effectively. To address this, it has a project to find ways of improving the usefulness of disclosures and in a recent Exposure Draft has included proposed amendments to two existing standards. One of these is IFRS 13 Fair Value Measurements. One controversial proposal that could affect valuers is to disclose reasonably possible alternative values. Consultation has now closed but both RICS and Valuology were among the respondents, both objecting to the practicalities of the proposals. The IASB received well over 100 comment letters in total, although many were concerned with the overall principles proposed for all disclosures rather than the specific proposals for IFRS13. The Board is scheduled to consider the responses received in Q2 2022.

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The public benefit conundrum

It says something about a common characteristic of governments of every type and persuasion that while over 150 nations have mandated their private sector organisations to use IFRS for financial reporting, or national standards that are closely based on IFRS, there is no such consistency in the way they present their own financial performance. Notwithstanding, there have been International Public Sector Accounting Standards (IPSAS) in place for many years. These are not yet widely adopted by national governments but their development provides a useful forum for debate on how the generally accepted principles in IFRS can be applied to the public sector. A long running project is to establish principles for how the public sector should measure assets created and held for the delivery of public services. One current proposal is to introduce a concept of Current Operational Value (COV). Following consultation in 2021 the IPSAS Board has received mixed responses to this. In our view there is a need for a specific modification of Fair Value in IFRS for public sector operational property but we were not happy with some of the detail around COV in the exposure draft.

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Value in the courts

It is rare for a year to pass without judges having to consider valuation issues and 2021 was no exception. We have picked the following out from the Courts in England and Wales:

- There have been two further cases where challenges have been brought against insolvency office holders by disaffected borrowers alleging that property was sold under market value. Both *Serene Construction Ltd v Salata and Associates* ([2021] EWHC 2433 (Ch)) and *In the matter of One Blackfriars Ltd* ([2021] EWHC 684 (Ch)) dismissed claims that development sites had been sold at below their true value because the receivers on the one hand and administrators on the other had not acted reasonably. However both confirmed the established principle that such office holders owe a duty to the borrower and any other creditors to obtain the best price reasonably obtainable. What is reasonable depends on the circumstances and both judgments indicated that this was not necessarily the same as the market value that could be obtained in other circumstances. However, they underline the point that valuers cannot sensibly opine on the price that it would be reasonable to accept for the sale of property held as security by or on behalf of a lender without knowledge of the circumstances under which the sale is taking place, especially any actual constraints on the seller.
- While attracting attention from lawyers because it departed from the established method of calculating damages because of what the Court of Appeal considered to be the unusual facts of the case, *Hart v Large* ([2021] EWCA Civ 24) also provided a useful reminder for valuers on the need for care when making assumptions. The valuer/surveyor in this case stated in their terms that they would assume that an inspection of those parts they could not inspect would not identify significant defects or a cause to alter their valuation. During the inspection there was no evidence of a problem but later severe damp problems emerged. In the report the surveyor advised that there would be damp proofing in place even though it was not visible. The Court held that the absence of any evidence of proper damp proofing coupled with the exposed location should have put the surveyor on enquiry as to whether the standard assumption was reasonable. A more detail summary can be accessed below, but the essential message for all valuers is that contractual assumptions must be reasonable will not protect you if there is evidence to the contrary that you should have noticed.

More Information

Please Get in Touch

We help firms and organisations ensure that they provide or receive valuations that are compliant with the applicable standards, maximise quality and minimise risk.

If you would like to discuss how we might be able to help you please do not hesitate to contact us.