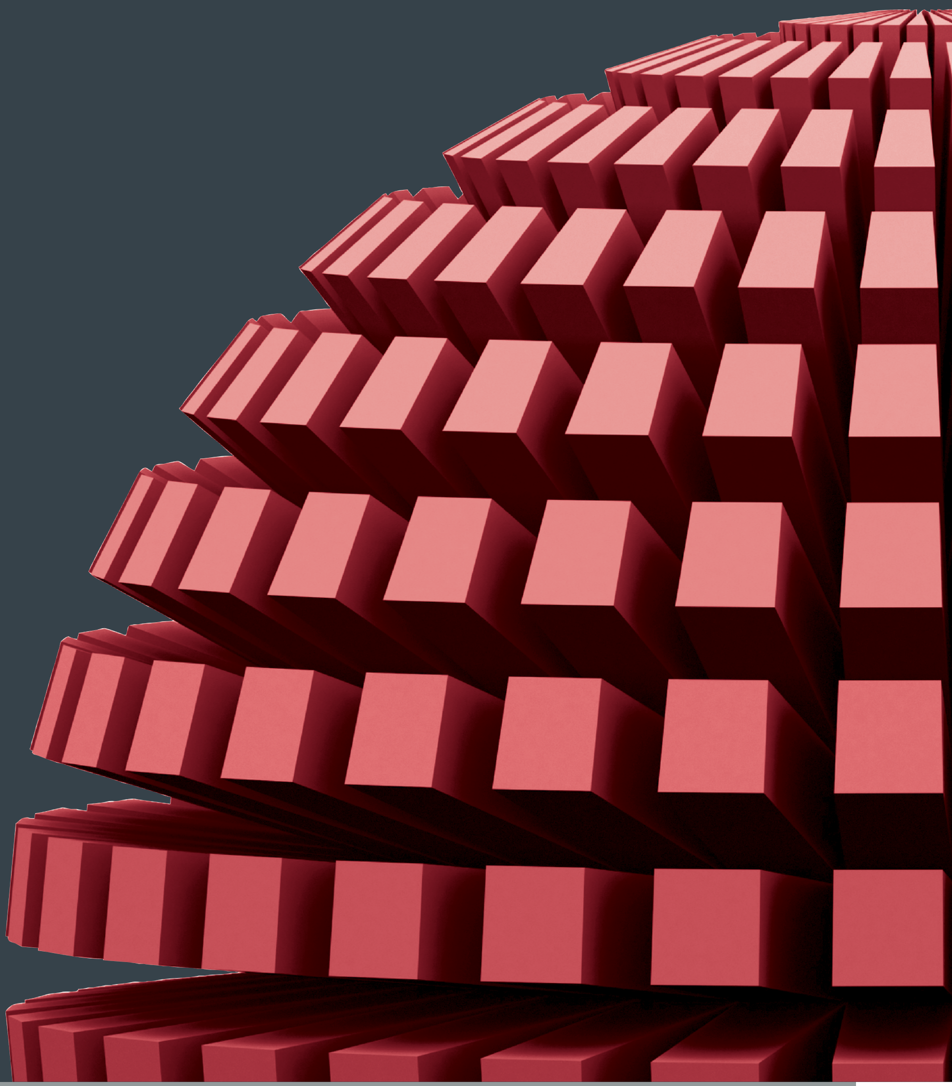
REPORT



RICS Valuation – Global Standards: UK national supplement

Basis for conclusion: UK VPS 3 only

October 2023

RICS®

Contents

Introduction

1 Responding to concerns over the reliability of valuation, perceived lack of valuer independence and rapidly changing market dynamics, the RICS Standards and Regulation Board (SRB) commissioned the Valuation Review to futureproof practices in the valuation of real estate assets for investment purposes, in the public interest. The purpose of the review was to assess where changes may be necessary to re-establish public trust in such a fundamental sector of the UK economy.

2 The Review was largely UK-focused and principally looked at valuations upon which third party reliance is placed. These valuations are subject to a number of specific requirements set out in RICS Valuation – Global Standards: UK national supplement, UK VPS 3.

3 The revised UK VPS 3 standard published alongside this basis for conclusions addresses the regulatory changes required to implement the Review's recommendations in a balanced and considerate manner. The updated standard has been approved by the RICS Knowledge and Practice Committee (KPC) and the SRB.

Approach to consultation analysis

4 The consultation responses and issues outlined here have been prepared to support and evidence changes to UK VPS 3.

5 In addition to consultation responses provided through the RICS i-consult platform, we have also considered evidence sent via email, as part of expert working groups and in one-to-one client and valuer insight sessions. This additional evidence is also included in this basis for conclusions.

6 The sections of this basis for conclusions cover the following key topics:

1 – Definition of Regulated Purpose Valuation (RPV)

2 – Public sector valuations and RPV

3 – Charities sector valuations and RPV

4 – Rotation policy (UK VPS 3.3)

5 – Involvement of independent client parties (UK VPS 3.4)

6 – Preliminary advice (UK VPS 3.5)

Summary of post-consultation changes

7 RICS and its boards and working groups have listened to the extensive and insightful feedback and have made a number of post-consultation changes. These were made to address potential negative market, business and consumer impacts referred to in the responses. We have also taken the opportunity to clarify and simplify certain elements (such as the rotation transition policy) further to the suggestions.

8 The post consultation changes are, in summary:

a The client anchor for rotation being the asset (as opposed to, for example, the client's parent company).

b A maximum period of ten years before the rotation of a valuation firm. This might include multiple engagements.

c A maximum single engagement period of five years.

d A maximum period of five years before the rotation of an individual 'responsible' valuer.

e A minimum three-year break after rotating off an engagement.

f The exclusion of all public sector valuations (local authority, central government and government agencies).

g UK VPS 3.3–3.5 to only apply to a subset of valuations for financial reporting under VPGA 1.

h An ability for valuation firms to notify their firm's responsible principal and RICS Regulation that they are not adhering to the normal rotation policy due to exceptional circumstances.

i Changing UK VPS 3.4 from the valuer 'verifying' to 'checking' the involvement of independent client parties in the instruction.

j Aligning UK VPS 3.4 with Rules of Conduct requirements on data – removing explicit limitations on valuation data.

k Simplified transition policy.

l Removal of the current UK VPS 3.2 requirement to forecast fees from the subject client.

Key consultation topic 1: Definition of regulated purpose valuation (RPV)

General summary of responses on RPV definition

9 The consultation proposals suggested two amendments to the RPV definition in UK VPS 3, to clarify what fell into scope of the additional proposed UK VPS 3 requirements (i.e. rotation and governance requirements).

10 The key proposals consulted on were to clarify:

i that secured lending valuation is excluded from the definition of RPV, and

ii RICS' position that the RPV scope included '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'.

11 The majority of responses (57%) either agreed or partially agreed with the definition of RPV, but there were a number of suggestions and requests for clarification, reflecting a lack of consistent understanding over the existing RPV definition. The consultation centred on four questions.

i Should the definition include or exclude secured lending?

ii Is the existing RPV definition appropriate in light of the more stringent additional requirements in the new proposed sections 3.3–3.5?

iii To what extent are public sector asset valuations already included in the RPV definition and/or should be in future?

iv Should the RPV include charity sector asset valuations?

Secured lending

12 Secured lending is not currently an RPV, although this is not explicitly stated in the 2018 version of UK VKPS 3. The consultation draft clarifies its exclusion but draws attention to guidance content at, for example, UK VPGA 10 – Valuation for commercial secured lending purposes.

13 The UK VPS 3 consultation received two responses from commercial secured lenders. Neither commented directly on the scope of the RPV definition, but both commented on the rotation proposals. One suggested they should be advisory within a secured lending specific section, the other that they should not apply to secured lending at all as they felt this was a different valuation process when compared to, say, fund valuation.

14 The only other comment on RPV scope in the context of secured lending came from a major valuation advisory firm, with the following suggested amendment to the definition:

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

15 The suggestion to amend this section improves clarity, so we have amended UK VPS 3 while noting UK VPGA 11 is now proposed to be valuation for (general) residential purposes as opposed to a mortgage specification.

16 Further to the consultation responses and other engagement we have decided to exclude all commercial secured lending valuation from the regulated purpose definition. Instead, we will cover secured lending in specifically tailored advisory material in VPGA 2 (all secured lending, globally), UK VPGA 10 (commercial) and the proposed separate residential secured lending guidance.

RPV definition and the application of new rotation and governance requirements

17 The consultation elicited questions from a number of respondents relating to the scope of applicability of mandatory rotation and the other proposals relating to valuer independence, along with concerns that the proposals potentially widen and over-expand the scope of Peter Pereira Gray's original report.

18 The definition of RPVs includes valuations carried out for financial reporting under UK VPGA 1. A number of responses referred to the breadth of financial reporting and suggested a focus in the Valuation Review on a narrower subset of financial reporting purposes – principally in relation to funds, institutional investment and in respect of UK Public Interest Entities (PIEs).

19 Although there was broad agreement to include financial reporting within RPVs, some respondents thought the definition should not only refer to valuations undertaken in accordance with UK VPGA 1, but also include reference to the IAS/FRC definition of investment property and/or explicit reference to e.g. UK PIEs. Some thought it should be limited to investment property.

20 Some responses thought the RPV definition should primarily address the level of risk of conflicts. One respondent proposed the following test:

> ‘1. Is there significant third-party reliance?
>
> 2. Is the company commissioning valuations a public entity?
>
> 3. Do valuations drive or influence buy/sell decisions?’
>
> Response from a valuation advisory firm

21 Insight from the audit sector also suggested that a test of third-party reliance was merited in the proposed rotation policy, along with considering whether the entity was listed (i.e. one in which the public could invest). The insight received from the audit sector cautioned against adopting an external definition of PIEs, as these are inconsistent across markets and subject to change (for example, the UK definition of PIES is different to the EU definition). They did suggest a further test of whether the asset/portfolio being valued was of material value when compared to the client reporting entity’s net asset value. It was accepted that such tests involved a degree of judgement. In the context of audit, this is based on the ‘objective, reasonable, and informed third party’ test, which is already an established concept in regulatory arrangements for auditors. They suggested a similar concept could be applied to valuation for assessing ‘materiality’.

RPV definition – impact

22 Some respondents suggested that the RPV definition in the consultation could place undue burden on small scale, ‘low risk’ financial reporting, which consultation responses suggested was not the intention or conclusion of the Valuation Review. Peter Pereira Gray was clear that any implementation needed to be proportionate.

23 The RPV consultation definition mainly focused on the purpose of valuation. Some respondents suggested there were more important points than this around, for example, third party reliance, scale of the operation, involvement of public entities, and risk to the public.

> '...there is a very real risk...that the RICS could over expand the recommendations from the Review to a much broader range of valuation types. This may not be in the valuation recipients' best interests or the wider public interest... The Review was focused on high-risk investment valuations for which we are broadly supportive of the findings and recommendations. However, low-risk operational valuations with limited third party reliance do not have similar concerns.'
>
> Response from a valuation advisory firm

24 It should be noted that the current UK national supplement includes an RPV definition and has established standards (UK VPS 3.1 and 3.2), to which the definition currently applies. The 2019 definition does not, for example, limit the scope of application to public interest entities. With this in mind, it is important to find a way forward that does not disrupt long-standing, existing requirements in UK VPS 3 applying to all financial reporting valuations (3.1 and 3.2), but equally does not inadvertently catch valuations in the current proposals that are not the intent of regulatory change.

25 To take account of the above, the scope of UK VPS 3 has been clarified to only include UK VPGA 1 and UK VPGA 2 considerations. Furthermore, the new UK VPS 3.3–3.5 standards (e.g. rotation) will only apply to a subset of clients – including large companies and those with transferable securities traded on a regulated market, e.g. REITs.

Key consultation topic 2: Public sector valuations and RPV

26 The UK public sector is generally considered to comprise central government (including all administrative departments of government, other central agencies and non-departmental public bodies, the NHS, HM Forces and academy schools); local government (including all local authorities as well as police forces in England and Wales) and public corporations comprising companies or quasi corporations controlled by government that receive more than half their income from market sales of goods or services.

27 Various respondents sought greater clarity on public sector valuations undertaken for financial reporting and which, if any of them, RICS intends to fall within the RPV definition.

28 The current definition of RPV includes valuations for financial reporting under UK VPGA 1. This section of the UK national supplement is wide-ranging and all-encompassing and, according to a key stakeholder's response, the UK public sector currently follows and adopts it, suggesting that public sector valuations undertaken for financial reporting are generally currently interpreted as falling within the definition.

29 The UK VPS 3 definition of RPV has never differentiated between private and public sector financial reporting in its application. However, it is clear from examination of various documents that RICS' original intent was that public sector valuations were excluded from the UK VPS 3 RPV definition, though it appears that this intention is not well-known by valuers and users of valuations in the public sector.

30 Peter Pereira Gray's review never specifically referred to the relevance of his recommendations to the UK public sector, but the public interest more widely was a key consideration. It is recognised that valuations for the public sector operate quite differently from the mainstream commercial sector and are ultimately controlled and subject to various rules beyond RICS' control.

Summary of responses

31 During the consultation, insight was received during roundtable meetings from a mixture of in-house and private practice valuers working for public sector clients, as well as accounting and finance professionals involved in instructing and commissioning valuations for local authorities. RICS also received six consultation responses in respect of the UK VPS 3.3–3.5 proposals from key public sector stakeholders including: CIPFA (The Chartered

Institute of Public and Finance and Accountancy), LGA (the Local Government Association), ACES (The Association of Chief Estates – Surveyors and Property Managers in the Public Sector), the Valuation Office Agency, as well as two private practices heavily involved in providing valuations to the public sector.

32 Of the six responses received from public sector stakeholders, none were overwhelmingly supportive of the revised UK VPS 3 scope and definition of RPV from a public sector standpoint: four respondents answered 'somewhat/partially', and two major stakeholders responded definitively 'no'.

33 Early in the consultation process, a major public sector valuation provider made the point that because UK VPGA 1 is also referred to elsewhere in the regulated purpose definition, and all of the public sector follows this while undertaking valuations for financial reporting, all of the public sector is effectively ruled into the mandatory rotation provisions as drafted for the consultation, whether this was the intention or not.

34 One valuation firm was of the view that RICS was potentially widening and overexpanding the original scope of the Review in its proposals. They also reiterated the point that all public sector valuations are ultimately controlled and subject to rules beyond RICS' control.

35 A recurring theme in four out of the six responses received was that there is little public interest benefit from mandating rotation in respect of public sector financial reporting valuations for investment properties, although there was some general support. One respondent valuer made the point:

> 'the decision to now treat local authority investment assets as RPVs is sensible...there is no reason why they should be treated differently to investment assets held by the private sector.'
>
> Response from a valuer

36 However, at the same time they were also of the view that regular procurement exercises in the public sector already ensured impartiality and prevented close and untested relationships developing.

37 One valuation firm considered that, in their view, there was an obvious conflict of interest situation arising from in-house local authority valuers valuing their own investment assets for financial reporting purposes:

> 'Whilst we appreciate the RICS may not have the authority to dictate Local Authority policy around Valuer appointments, we feel the matter could be addressed by excluding Registered Valuers employed by an organisation from undertaking regulated purpose valuations on their employer's behalf.'
>
> Response from valuation firm

38 One institutional response considered that the rotation proposals were '*onerous and burdensome*'.

39 Some responses made the point that there is less risk attached to many (particularly operational) public sector financial reporting valuations compared to those relating to the private sector and investment markets as there is often only tenuous (if any) third-party reliance. Also, the point was made that the valuations do not drive buy or sell decisions and are undertaken retrospectively, with no incentive for valuation figures to be artificially high or low.

40 A local authority organisation commented:

> 'The administrative cost of running procurement exercises in local authorities can be high and this cost may not outweigh the benefit to the local taxpayer... The consequence of further delays to the publishing of audited statements means that the usefulness of the financial statements is affected, which could be more detrimental to the users of the accounts than the perceived risks around valuer independence.'
>
> Local authority organisation response

41 One valuation firm also had concerns about the additional cost mandatory rotation would bring at a difficult time for the public sector:

> 'Moving to a system where such a valuation must be obtained for an external valuer would add a certain amount of cost and process to the system and so would need to be clearly justified, if adopted, particularly as the system for auditing local authority accounts is currently in something of a state of crisis. Anything that potentially makes that worse by adding a further complication to the accounts is unwelcome. At present I do not see a justification for such a change.'
>
> Valuation firm response

42 In respect of public sector-related responses, there was general support for these being applied subject to clarification of various practical aspects arising from UK VPS 3.4 and the need for potential amendments to tailor specifically to the public sector. One organisation made the following comments in this regard:

> 'In paragraph 1, clarification will be needed on what the expectation is in terms of the public sector equivalent of a 'non-executive director' and 'corporate compliance officer'. Similarly, in terms of the role of any 'independent chair of the firm's audit committee' it should be noted that in the case of local authorities, such committees are rarely chaired by an independent person, and generally chaired by an elected Councillor. Clarification on the equivalency will be needed. In paragraph 2, clarification will be needed on the equivalency in circumstances where the Member or Firm are in-house.'
>
> Response from membership body representing public sector valuers

43 Concerns were raised that implementing some aspects of the UK VPS 3.4 proposals were beyond the control of valuers.

Public sector implementation of UK VPS 3.3–3.5 – impact

44 CIPFA believed the administrative cost of running procurement exercises in local authorities can be high and this cost may not outweigh the perceived benefits of any further valuer independence to the local taxpayer.

45 The point was made that public sector financial reporting valuations are already subject to stringent audit requirements, so much so that there are already significant audit

delays in the auditing of these valuations. One valuation firm was of the view that the introduction of mandatory rotation provisions to public sector valuations could potentially cause disruption to valuation services of public sector entities, who are already subject to limited resources during a time of austerity and tightening of the public purse.

46 Further, the fact that internal valuers of local authority valuation teams are not themselves defined as RICS regulated 'firms' and are heavily involved in this process, potentially creates practical challenges in incorporating these valuations into the UK VPS 3 RPV definition. A further potential conflict highlighted is the extent to which these internal valuations are 'excepted' (or not) as per RICS Valuation – Global Standards: another grey area that directly conflicts with the RPV definition and provisions as drafted. Ultimately, public sector valuations are governed by central government rules that RICS has little control over. These important technical points themselves may prohibit potential and effective implementation of the proposed provisions.

47 Finally, certain aspects of proposed UK VPS 3.4 may be challenging to implement practically in the public sector and may be beyond the control of valuers. The drafting may require specific amendments to be made relevant for application to the public sector.

Summary of post-consultation changes made in respect of public sector

48 Further to consultation, changes were made to the UK VPS 3 regulated purpose valuation scope to clarify the complete exclusion of all forms of public sector valuations for financial, along with clarifying the complete exclusion of the public sector from the scope of UK VPS 3.3–3.5 proposals relating to rotation and independence proposals. This decision was made subject to further action of a dedicated workstream being commissioned for this area. RICS continues to liaise with key stakeholders to achieve this.

49 Subsequently, the scope of the VPS 3.3– 3.5 provisions were agreed to be narrowed to: 'only in respect of assets owned or part owned by entities whose transferable securities are admitted to trading on a regulated market or large companies (those that do not qualify as a micro entity, small or medium company as defined in section 381 to 384 of the *Companies Act* 2006)', which effectively excludes the public sector by implication.

Key consultation topic 3: Charity sector valuations and RPV

50 There are similar arguments to those set out above for the public sector about the extent to which charity related valuations undertaken for financial reporting are within or excluded from the scope of the Valuation Review. Because of the wide application of UK VPGA 1 and its inclusion in the RPV definition, these valuations may be covered by the proposed amendments to UK VPS 3.

51 The current UK VPGA 8 Valuation of charity assets provides guidance to valuers undertaking valuations relating to charities in addition to UK VPGA 1 Valuation for financial reporting: general matters. All charities must follow the Charities SORP (as periodically updated) that applies the Financial Reporting Standard applicable in the UK and Republic of Ireland (FRS 102).

Summary of responses

52 Two valuation firms, with extensive work undertaken in the charity sector, provided viewpoints specifically in respect of charity-related valuations. They both highlighted the need to exclude charity-related financial reporting valuations from the rotation and other independence provisions. One firm considered the proposals were:

> 'Inadvertently being applied to the valuation of assets for financial accounts which may be only valued infrequently and/or have low risk to stakeholders. The benefits of rotation in such circumstances are likely to be outweighed by additional and unnecessary costs……. The valuation does not drive buy or sell decisions (sell decisions are taken at asset level and are covered by the Charities Acts and buy decisions also requires separate acquisition advice). The valuation advice in these circumstances is again therefore more a retrospective measure of performance. Indeed, for certain of our clients, it is perceived as an exercise to fulfil an accounting function with the outcome of little or no practical use to them.'
>
> Valuation advisory firm response

Charity sector implementation of UK VPS 3.3–3.5 – impact

53 The administrative cost of running procurement exercises in charities can be high and this cost may not outweigh the perceived benefits of any further valuer independence.

Summary of post-consultation changes made in respect of charity sector

54 RICS looked at two options for considering charity related valuations for financial reporting under UK VPS 3:

- complete exclusion or
- some form of mitigation.

Complete exclusion was rejected on the balance of evidence, particularly noting that some major investors and asset holders have charitable status. A generic exclusion was considered to be too broad, given that the likes of universities, social housing providers and major organisations may be charitable organisations, and that charities can also exist as registered companies.

55 The scope of the VPS 3.3–3.5 provisions was agreed to be narrowed to: 'only in respect of assets owned or part owned by entities whose transferable securities are admitted to trading on a regulated market or large companies (those that do not qualify as a micro entity, small or medium company as defined in section 381 to 384 of the Companies Act 2006).'

56 One of the effects of this will be to exclude smaller charities while retaining governance around larger organisations.

Key consultation topic 4: Rotation policy (UK VPS 3.3)

Summary of responses

57 Some respondents disagreed with their sector's inclusion in the regulated purpose definition (e.g. some public sector stakeholders) and the subsequent obligation to rotate valuers/firms. Others thought the policy should be more focused on the level of risk:

> 'The nature and extent of the [rotation] Policy to be applied should depend on the significance of the threats to objectivity and independence. Where a threat is clearly insignificant, no rotation of valuers is needed, e.g. non listed or private companies'
>
> Valuation advisory firm's response

58 The majority of respondents (65%) agreed to the rotation policy included in the consultation to some degree, answering 'yes' or 'somewhat/partially', although this was predominantly the latter (57%), with only a few respondents fully agreeing to the proposals (8%). Further commentary on the frequency of the rotation cycle is included below.

Impact of rotation

59 Numerous respondents referred to the impact of the proposed rotation policy on business, in particular concerns about potential to reduce competition and its impact on investor clients via increased costs and less choice. Conversely, it should be noted that there were positive responses and comments about rotation and improved governance as well.

60 There was disagreement around the impact rotation would have on businesses. Some suggested there would be limited costs but this was outweighed by the benefits, and others saying that costs would be substantial, and benefits limited.

'[XXX] anticipate there will be a cost of implementation to clients due to procurement and onboarding of new valuers but that, in the context of the overall value of the portfolios, and the purpose for which the valuations are being prepared, this cost is not material....[xxx] are aware that a number of clients already rotate every 3 years and cost is not considered a material issue. The positive impact in terms of enhanced trust in the profession more than outweighs any short-term cost of implementation.'

Valuation advisory firm

'Retendering and onboarding new valuers is a significant cost.'

Asset manager/developer response

'Changing valuers has a significant business impact in terms of the time and resource incurred by both the client and valuation firm.'

Asset manager/developer response

'[The cost is] marginal from a unit/shareholders perspective in the context of Investment Management Agreement fees.'

Investment manager response

Rotation cycle

61 The most frequently referenced issue was the term of the rotation cycle. Only three respondents fully agreed to the five plus three years proposed in the consultation. All respondents who did not agree suggested their own variation on the terms, for example, service reviews, the dynamic between members and firms, and whether it was advisory or mandatory. Excluding the detail of these variations, a basic summary of the suggested frequency, where referenced by respondents by respondents was as follows:

Suggested term	Responses
5 to 6 years	5
8 years (or 5+3 years)	5
10 years +	6

62 One respondent suggested maintaining the advisory Red Book Global Standards term of seven years as the only RICS valuation rotation policy. Some respondents suggested that measuring rotation by time periods was incorrect, for example, one respondent suggested that four valuation occurrences was a better test.

63 The suggested alignment of rotation frequency with the audit profession was cited in 14% of responses – including from client and valuer stakeholders (a theme also seen in the earlier Call for Views). Statutory and professional audit standards allow a 10-year term for firms, with the option to extend by a further 10-year term subject to a retender (potentially a maximum of 20 years). Within this term, audit partners must change every five years (can be extended to seven years in exceptional circumstances). Reasons given for valuation aligning with audit in respect of rotation cycles principally related to the impact on business (cost, disruption and resource).

> ‘Our reasoning for UK VPS 3.3 to mirror the existing rules on auditor rotation are:
>
> a. This would give consistency between the audit and valuers rotation rules and minimise client confusion as to contractual relationship periods.
>
> b. There would be reduction in the disruption of the set-up period for valuers undertaking frequent (often monthly) valuations of portfolios.
>
> c. There would be a reduction in the friction costs for clients and valuers associated with the changeover of valuation firms. It would provide a longer period of certainty for valuers in order to build and maintain the large valuation teams required to undertake frequent valuations. This is important where valuers are required to undertake detailed DCF valuations and analyse comparable evidence using the same methodology.’
>
> Trade body for funds response

64 Feedback from the audit sector suggested that RICS proposals were not unreasonable and that it was not necessary to mirror the audit rotation cycle and structure per se. However, they did refer to the fact that the five-year cycle applies to audit partners whereas the ten-year cycle relates to audit firms. This in most cases achieved a natural symbiosis as the two cycles fitted into each other, although it was noted there is flexibility within this.

65 Further research on audit rotation undertaken by RICS suggests no compelling technical reason why it should be exactly aligned with valuation and was inconclusive on the benefits or otherwise of the audit rotation terms.

Property market cycle and rotation

66 Noting the extensive commentary on rotation cycles and frequency in the consultation responses, the RICS Chief Economist was asked to comment on the average term of UK property market cycles to see whether this could provide further insight. He contacted two research partners and they suggested that 12–14 years was an appropriate figure when using the occupier market as the benchmark. If looking at yields/capital values, it was more like 10 years. It is worth noting that one researcher suggested that the gap between troughs appeared to be a shortening – perhaps indicative of a more connected world and/or shortening lease lengths.

67 Though the rotation cycle could not be timed to align with market cycles, it was noted in previous insight for the Review that particular pressure on valuers is applied when the market is rapidly changing or restructuring (positively or negatively). Therefore, when considering the proposed rotation frequency, it is useful to reflect upon the number of likely pressure points across a rotation cycle.

68 The proposed rotation cycle is not unreasonable when factoring in the frequency of property cycles, though there is an argument that a slightly longer rotation cycle could be justified on this basis.

Break between rotation cycles

> ‘We do not consider that there can be any regulatory justification for the requirement for there to be a “fire” break of at least five years between an instruction. As we said in our previous consultation response, we consider this to be anti-competitive. In our view, a break of not less than two years would be adequate to meet the regulatory intent of this provision.’
>
> Valuation advisory firm response

> ‘In particular, the 5 year lock out is excessive which unduly restricts choice. For clients who award split mandates to numerous valuers for governance reasons, it is wholly unworkable.’
>
> Valuation advisory firm response

69 A number of respondents also commented on the five-year break between rotation cycles, with some of the view that this was too long a period and had not been justified in the wider discussions and commentary. Some suggested that the break should be shorter depending on the level of risk and the outcome of other governance measures such as a service review. A valuation advisory firm suggested a four-year break, an asset manager three years, and another valuation firm not less than two years. Another valuation firm suggested that the proposed ‘fallow period’ was unreasonable when compared to the maximum eight-year term. Taking this feedback into consideration and looking at the context of wider consultation changes summarised in the introduction, RICS has concluded that a three-year break supports the aims of the Review, whilst addressing the concerns raised.

Service review

70 There were numerous comments made about the timing, nature and application of the service review. Auditor respondents raised concerns about their role in the service review process and potential conflicts with their own regulations/processes. Others asked why the service review test was only undertaken at the fifth year, rather than on an ongoing basis. Some suggested that the service review provision as drafted could be circumnavigated/ineffective and would create an actual rotation cycle of eight years (which was argued by one respondent as not forming part of the Review recommendation as it referred to five years and nine years for lower risk valuations). With reference to this specific consultation evidence and looking at the overall desire amongst respondents to simplify and clarify the overall approach, RICS removed the service review provisions suggested in the consultation draft.

> '[We] anticipate that there could be risk implications for a client's auditor if they were tasked with inputting into a service review and whether they would agree/approve the continuance of the provision of valuation advice from the current advisor. We anticipate that the auditor may not wish to take on this risk/liability.
>
> The wording re rotation, service review etc. is somewhat confusing, and it may be open to interpretation. Might it be supported by a 'decision tree' or 'flow diagram' to clarify timings, etc?'
>
> Professional services provider and 'big four' auditor

Definition of client for purposes of rotation policy

71 It was suggested by a number of respondents that if 'client' meant the overarching firm and all related entities, rotation could quickly become impractical as, after the first rotation cycle, they would have to change all of their valuers and would be limited in terms of choice for replacements.

72 Several responses from client and valuer stakeholders queried whether the term 'client' should be taken to mean a corporate entity and all related entities (described by some as 'firms') or alternatively an individual fund, portfolio or other asset group. Some respondents thought it should be the latter rather than the former for rotation, with particular impacts referenced by large multi-fund asset management firms.

'[XXX] is supportive of a rotation policy which requires changing the valuers of a specific asset/portfolio of assets after a fixed period (TBC) and indeed we already have such an internal policy.

However, if the restriction is applied to the firm level, rather than the valuation of specific assets, there are several practical issues which make it unworkable in our view:

- for an organisation such as [XXX] with multiple JV partners (who would themselves have the same restrictions) it would be challenging to find an appropriate valuer that neither party has used for valuations in the last 5 years.
- the transition would be particularly challenging – regardless of the time period, it would require many organisations to cease all instructions with current valuers and identify other valuers that have not previously been used who have sufficient competency and experience of taking on a large portfolio. As we, and others, currently hold instructions with the largest firms, this would prevent us from using these going forwards, and we do not believe that, at this moment, there are a sufficient number of valuation houses of sufficient scale to make this possible.
- Applying such restrictions reduces the pool of potential valuers that a company is able to instruct, reducing competition and in the worst cases (where few firms have capability/capacity) it would make fee negotiations uncompetitive.'

Response from a valuer at an asset manager

73 A number of institutional owners of investment property referred to their own current commissioning policies, including how they rotate valuers across funds/portfolios and manage relationships appropriately through the use of panel management*.

74 In analysing the consultation evidence, RICS felt the 'client definition' issue could be a major impediment to the proper functioning of a mandatory rotation policy. Further analysis and options were discussed with an expert working group and in detailed interviews with client and valuer stakeholders. The result of this analysis was changing the 'anchor' for rotation from the client entity to the asset – which was agreed to be more practical, identifiable and ultimately workable.

*A valuation panel is where a firm has a policy – usually in the form of a framework or service level agreement – that allows for the instruction of valuations from a pool of valuers with expertise in the relevant sector/location/purpose. An option around panel management is included below.

Provisions where no valuation firm is available to enable rotation

75 Concerns were raised by a number of respondents about specialist markets, for example affordable housing and unusual locations.

> ‘the rotation piece...doesn’t provide for circumstances where there are very few specialists valuers and so the mandatory rotation might not be so easy to achieve in practice if there are not sufficient alternative forms in the market. E.g. if a client goes to tender as the time is up but can’t identify any suitable alternatives what steps are to be taken then? I expect this only applies to a minority of valuations but could there be some guidance added for that? I know that clients often struggle for choice in some locations/sectors. All valuations should now have a cashflow framework to them – grounded in the transaction evidence.’
>
> Response from a valuation advisory firm
>
> ‘VPS3 should contain an additional provision, which provides for the client and the valuation firm to jointly apply to the proposed Valuation Committee (which when formed will sit under the [SRB]) for a dispensation, or partial dispensation, from the mandatory rotation requirements under extenuating circumstances. Such circumstances would need to be genuinely “extenuating” and the decision as to whether or not to grant the dispensation should be in the absolute control of the Valuation Committee. As an example, this might be used in circumstances where the client has been unable to find another firm who can (or is willing) to provide a particularly specialist valuation service.’
>
> Valuation advisory firm response

76 In many cases the concerns around specialist markets are alleviated by the proposed transition policy and are further mitigated by removing public sector and amending the rotation policy to limit it to a narrower range of circumstances (e.g. large companies) . However, it is recognised that there may be very occasional situations where, for a number of reasons, including the nature of assets to be valued, the pool of valuers is very limited or even situations where there is no alternative valuer available despite a thorough market search.

77 It is therefore important to consider the provisions for a situation where only one valuer is available and they are caught by the rotation policy, and to avoid the situation where an entity cannot comply with its statutory reporting obligations due to the inability to find a valuer. However, clearly any such arrangement must include provisions to prevent it becoming a loophole to the general policy. A suggestion by one valuation firm was for the proposed RICS valuation assurance committee (VAC) to be involved in this process. In response to the evidence from stakeholders, the proposed post consultation changes now include a mechanism for mitigating the ‘exceptional circumstances’ risk, with safety mechanisms involving RICS regulation and client confirmation to avoid this being used illegitimately.

78 Further to the extensive and wide-ranging feedback on rotation we have had to take a balanced view that allows for practical implementation while maintaining and improving professional standards. This feedback and review led to key decisions as referenced in paragraph 8 being implemented.

79 These key decisions allow for the mandatory rotation of both valuers and regulated valuation firms at a reasonable frequency and with as limited negative market impact as possible.

Key consultation topic 5: Involvement of independent client parties (UK VPS 3.4)

Summary of responses

80 The majority of respondents (59%), at least partially agreed to the UK VPS 3.4 proposals for valuers to involve independent client parties in the instruction and engagement process, while 16% disagreed. One respondent asked whether an internal compliance officer was suitably independent. Several respondents, while agreeing safeguards around instructions and terms of engagement were needed, thought that they could cause administrative burden and cost if they were not appropriately designed.

Limitations

81 Some thought the UK VPS 3.4 proposals were impractical, with some valuer respondents noting that the regulation of the process was targeted at them but ultimately relied on the actions of the instructing client. A potential solution is for valuers to be mandated to undertake reasonable checks of independent client party involvement in the instruction process – but not for them to have to 'audit' the client-side involvement. It would then be a matter of reasonable professional judgement as to whether the client response was satisfactory. On further analysis of the evidence and in light of consultation responses, RICS agrees that valuers are not in a position to fully 'verify' independent client party involvement but that they should at least ask relevant questions. The post-consultation standards have been changed accordingly.

> 'This is very onerous and not required. A director of the instructing client should be sufficient. If it is decided that this is required, then as noted before we believe that where an independent valuation committee / internal valuation team exists they can also take on the role. Within [xxx] they sit in the finance function, physically separate from the investment teams and are separately renumerated.'
>
> Pension fund 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.’
>
> Valuation consultant

82 Note some asset management/developer responses either didn’t have a strong opinion on this issue or were supportive and had similar measures in place already.

Key consultation topic 6 – Preliminary advice (UK VPS 3.5)

Summary of responses

83 Most respondents supported greater governance around preliminary advice, draft valuations and meetings with clients during the valuation process. The majority of respondents at least partially agreed to the proposed wording (59%), while 16% disagreed.

84 Numerous respondents sought clarity on whether this provision referred to the valuer or client. If the latter, similar responses were given as to UK VPS 3.4, noting that this would involve a valuer placing an obligation on a client, something some respondents thought went beyond the reach of RICS standards and regulation. These responses have been taken into account, with the standards amended to clarify that it refers to the valuer.

85 All six of the respondents who disagreed with the proposal referred to the impracticality of involving independent client parties in sign off of preliminary advice. This was also referred to by a further eight respondents who partially or somewhat agreed with the proposals. In response to this evidence and wider concerns about the limitations on a valuer's ability to mandate requirements for clients, the section has been substantially amended and shortened, to focus on the valuer's role.

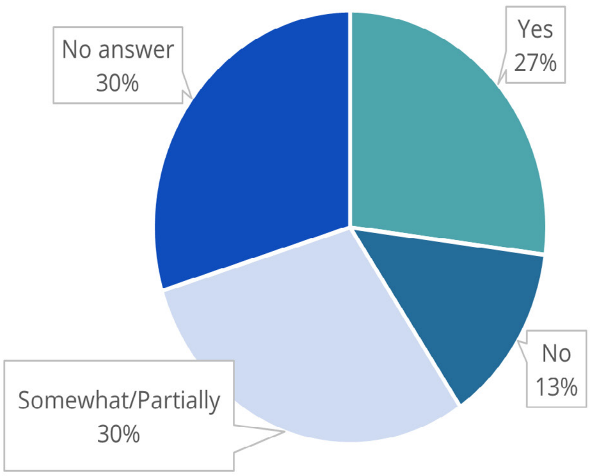
86 A number of respondents referred to extending/changing the obligation so that it more explicitly formed part of the reporting process, rather than being a 'file note'. It was not felt that this step could be taken at this time on the balance of evidence. The element requiring that the 'record must be made available to auditors or any other party with a legitimate and material interest in the valuation.' is retained, which is considered to sufficient.

> '[xxx] is in support of the new UK VPS 3.5 but feel the RICS could further strengthen the requirements around best practice and make it part of the valuation reporting process and encapsulated within the valuation report ultimately issued by a valuer.'
>
> Valuer response

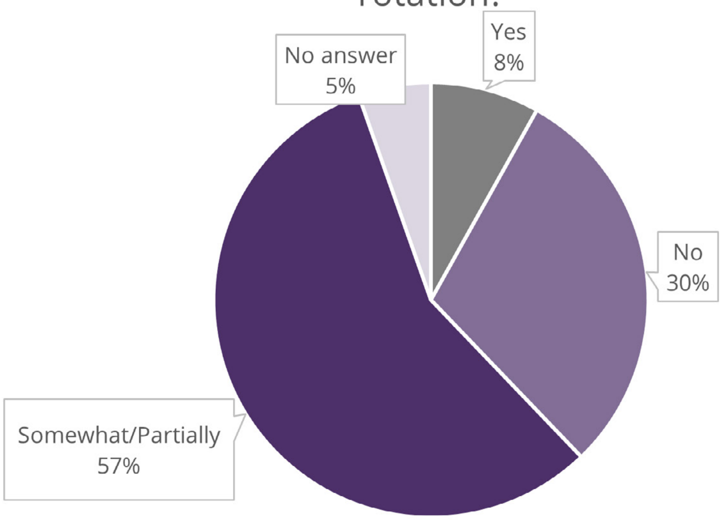
> 'A difference report should be included within the minutes and made available to 3rd parties.
>
> This sets out the valuation assumption differences between the 1st draft and final figures. Again, this will aid transparency over client pressure.'
>
> Investment advisory firm response

Statistics on specific consultation questions

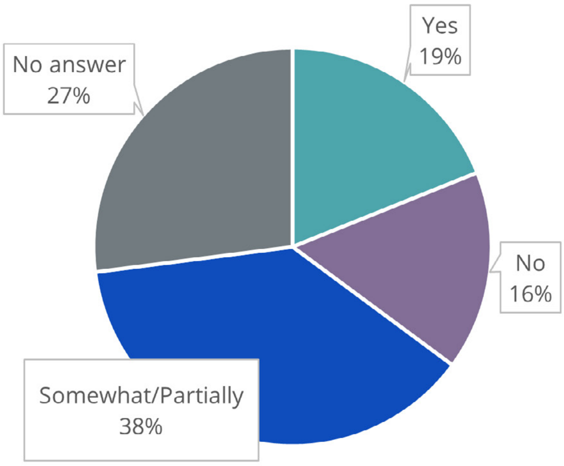
Do you agree with the revised UKVPS 3 scope and definition?



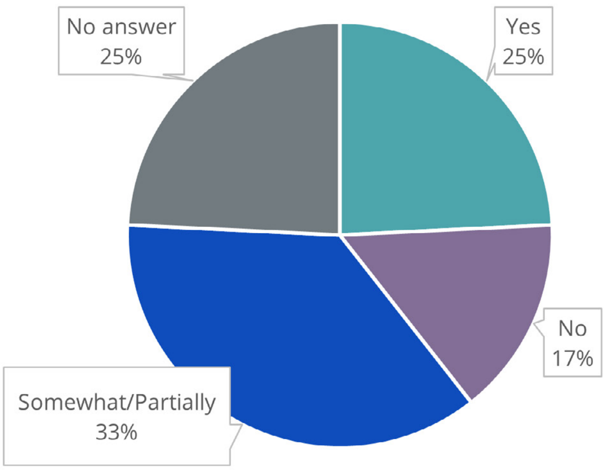
Do you agree with the proposed UKVPS 3.3 covering rotation?



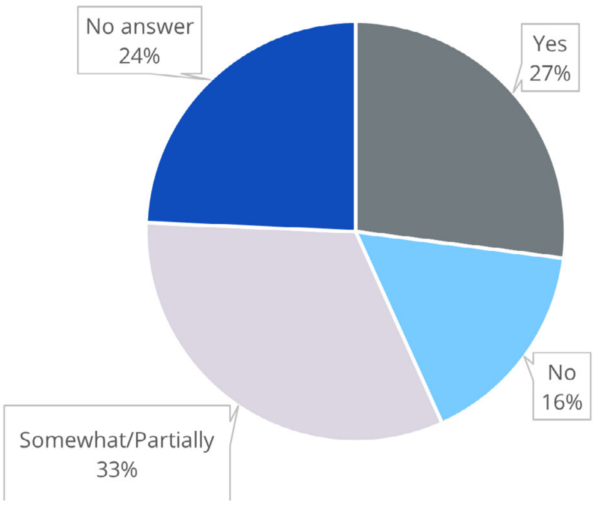
Do you agree with the proposed rotation transition policy?



Do you agree with the proposed UK VPS 3.4?



Do you agree with the proposed UK VPS 3.5?



Delivering confidence

We are RICS. Everything we do is designed to effect positive change in the built and natural environments. Through our respected global standards, leading professional progression and our trusted data and insight, we promote and enforce the highest professional standards in the development and management of land, real estate, construction and infrastructure. Our work with others provides a foundation for confident markets, pioneers better places to live and work and is a force for positive social impact.

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