Independent Review of Real Estate Investment Valuations

Peter J. Pereira Gray

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Chair's Introduction

I am honoured to have been asked to lead the Independent Review of Real Estate Investment Valuations ('the Review') for the Standards and Regulation Board of the Royal Institution of Chartered Surveyors (RICS).

Much of the world's wealth consists of the value of real estate.[1] Land and buildings are therefore important global assets, against which much international financing rests. Property values can therefore literally be said to underpin the finances of society.

The valuation of investment property is therefore of the utmost importance, not just for professionals striving to provide high-quality valuations for their clients and their observers, but for society at large.

An unchecked loss of confidence in the valuation of investment properties could therefore give rise to national-level systemic risk.

This Review is therefore of real consequence, and I am pleased to make a series of recommendations that I believe will improve confidence in property investment valuations, and the process by which they are undertaken and reviewed around the world.

The Review has been commissioned by the RICS Standards and Regulation Board, but it is of course written for all the valuers working around the world, for clients instructing and receiving the reports, for investors and financiers acting upon the outputs, and for the regulators overseeing the whole system. Genuinely, it is for all of us.

If society sleeps more comfortably at night knowing that its finances are more secure, this work will have been most worthwhile.

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1 McKinsey Global Institute, *The rise and rise of the global balance sheet: How productively are we using our wealth?*, November 2021. This can be found here: https://www.mckinsey.com/industries/financial-services/our-insights/the-rise-and-rise-of-the-global-balance-sheet-how-productively-are-we-using-our-wealth

Introductory Comments

Trust is the essential ingredient in supporting the role of professionals in society. It is therefore trust that we must seek to bolster as we consider recommendations that might make property investment valuations more robust for their users: those that instruct them, those that undertake the work, those that receive them, those that analyse them, and those that oversee and regulate them.

Trust in professionals, and the positive reputation that normally goes with trust, relies upon there being confidence in both the competence and the ethical conduct of the professional. Competent clients need to be able to instruct competent valuers and receive a competent service. Trust in the competence of individuals providing a service lies in the independent observation and the quality assurance provided by those overseeing the assessed activities. In the context of this Review, all the professionals involved in property investment valuations need to be competent, and to be seen by others to be so.

The RICS Standards and Regulation Board has asked me to make recommendations in relation to property investment valuations. It asked that I consider valuation methodology, property risk analysis, independence and objectivity, and measuring market confidence in valuer performance, with the overall aim of underpinning trust and confidence in the valuation profession.

In this Review, I have engaged with a wide variety of stakeholders with my Expert Advisory Group (EAG), a Call for Evidence, roundtables, and direct engagement with key industry figures. I have also undertaken a literature review and applied my own understanding and experience of valuation to ensure that the findings and recommendations I make are as robust as possible.

The initial evidence gathering for this Review looked at all aspects of valuations of property assets for investment purposes, but my attention has been primarily focused on valuations of real estate assets for performance measurement and decision-making purposes, upon which third parties place reliance. These are principally valuations for:

- financial reporting
- inclusion in prospectuses and circulars, and takeovers and mergers
- collective investment schemes
- unregulated property unit trusts
- commercial investment property financing

It is this category of high-risk valuations where third-party reliance is critical, and where public confidence must be at its highest. Consequently, it was this group of valuations that were the main driver for the majority of the recommendations within this Review. Ultimately, the narrower nature of immediate reliance – such as residential mortgage valuations for private homes – has not been central to my consideration. I must stress that this is not to suggest that collectively these valuations are not of systemic importance to the economy and to confidence in the profession, but simply that they were not the central focus of this Review.

Nonetheless it is my wish that, where appropriate, relevant principles identified in this Review are extended to all valuation work, whilst ensuring that proportionality is carefully considered in the application of these recommendations and any resultant stipulations made by RICS.

I note the substantial progress that RICS has made over the past 10 years and more to create a respected professional framework for valuation under the independently-led oversight of the RICS Standards and Regulation Board. Notably these include the creation of valuer registration and compliance monitoring, the bolstering of its enforcement processes, and the maintenance of the Red Book as the preeminent standard of its kind.

Throughout the Review, I have kept in mind the RICS Royal Charter and the role of the profession in society. I have approached this Review from the perspective that the culture and behaviours of the professionals involved in the valuation of land and buildings should therefore be held to the very highest public standards.

This Review has been largely UK-focused but I have at all times kept in mind the global role of RICS, and am keen to see RICS develop and monitor standards globally so that progress can be improved over time in regions of the world that are currently less developed.

Executive Summary

Property matters to society. The net worth of society has been estimated to have tripled in the last 20 years, with the increase mainly reflecting valuation gains in real assets, especially real estate.[1]

Land and buildings provide the social spaces in which society lives, works, and plays. The same land and buildings that provide the physical infrastructure of society also, by virtue of their value, play a critical role in the financial underpinnings of society.

Greater value lies in residential land and buildings, but the valuation of investment property is therefore of critical importance, not just for professionals striving to provide high-quality valuations for their clients and their observers, but for society at large.

Significant amounts of international financing effectively rest on the correct assessment of the value of land and buildings, so these property values literally support the finances of society.

A loss of confidence in the process of investment property valuation and its outputs could potentially undermine confidence and could give rise to national-level systemic risk.

This Review comes at a time of great societal change and a perception that all is not well in the area of property investment valuations. The Review is therefore intended not just to enhance the process by which valuations are arrived at, but also to guide the governance of the process to ensure it remains appropriate for a changing world.

Supported by an Expert Advisory Group (EAG) handpicked for their expertise and ability to contribute, I engaged with a wide cross-section of those involved with property investment valuations from across the globe. There were many virtual meetings with correspondents and follow-up calls where appropriate.

Particular concerns around independence and conflicts of parties involved in property investment valuations were highlighted as matters for our attention early on in the Review, and it became clear that there were further issues to consider, beyond the initial terms of reference, and these were going to be critical to the Review outputs. We therefore broadened our considerations to accommodate these wider factors.

As a consequence of our review, the EAG and I have noted several matters in current valuation industry practice that we feel could be improved, and I make a series of recommendations to the RICS Standards and Regulation Board.

With the support of the EAG, I make 13 core recommendations. Of these, there are three key recommendations that overarch all of the others, and that I bring to particular attention here.

1 McKinsey Global Institute, *The rise and rise of the global balance sheet: How productively are we using our wealth?*, November 2021.

I recommend:

i. The creation of a dedicated, independently-led valuation regulatory quality assurance panel, under the jurisdiction of the RICS Standards and Regulation Board.

ii. The creation of a formal Valuation Compliance Officer role within regulated valuation providers to ensure services are delivered appropriately, objectively, and to the standards observed across today's financial services industry. This role is envisioned to provide a robust foundation for full accountability and responsibility of valuation firms to their clients and to the valuation regulatory quality assurance panel, particularly where multidisciplinary services are provided to clients.

iii. The need for further specific RICS guidance to clarify RICS' expectations around the culture and behaviours expected of RICS professionals in the pursuance of valuation activities.

Whilst these three recommendations offer an overarching framework for a way forward, they are not the only substantive recommendations.

I have also concluded that the discounted cash flow methodology should become the primary mechanism for deriving valuations going forward, that valuers should be subject to a mandatory rotation and revalidation programme, and that there should be improved standards for communications between valuer and client.

In a conclusion that will please some and frustrate others, I have concluded that multidisciplinary service providers may still undertake valuations, but they need to be supported by a robust compliance function built into the service delivery to protect everyone from the conflicts that can arise around a valuation process.

There is a clear need to see education standards move with the times, especially in support of the recommendation to use discounted cash flow as the primary valuation methodology going forward.

I have found the Red Book to be a sensible document that is regularly updated, but I feel that a more digestible short-form version would be helpful, especially for clients.

I would like to see clearer guidance from RICS on whistleblowing and a clearer framework for the provision of property risk advice, including separating it from the valuation service, especially if undertaken by the same practice or individual.

I would like to see client practices improve and I identify that there are clear opportunities to improve the commissioning and subsequent reporting of valuations.

Where possible – and especially in the field of regulated valuations – I would like to see non-executive directors take a more active role in managing information and conflicts. I believe that the creation of a formal audit trail of communications between client and valuer would help significantly in this regard, as would access for both client and valuer to the valuation regulatory quality assurance panel.

Over and above the key recommendation that RICS considers the culture and behaviours of participants in the matter of property investment valuations, I would additionally like to see RICS recognise the further opportunities that arise from embracing diversity and inclusion policies widely across the profession – and specifically in the valuation sector.

The full list of recommendations is as follows.

Recommendation 1 – Commissioning and Receiving Valuation Reports
RICS should work with appropriate stakeholders in standardising governance arrangements for commissioning and receiving valuation reports for high-risk and 'regulated' valuations.

Recommendation 2 – Valuation and Advisory Activities
Valuers, with the support of RICS, should ensure that the separation of valuation from advisory activities within firms is consistently applied in respect of the use of valuation data and instructions.

Recommendation 3 – Rotation
RICS should develop a time-specific, mandatory procurement and rotation process for valuers.

Recommendation 4 – Compliance Role
RICS should build on its existing 'RICS responsible principal' obligation by developing a Valuation Compliance Officer role to specifically cover valuation process and conduct.

Recommendation 5 – Raising Concerns
RICS should ensure it has clearly signposted processes for its regulated members and other stakeholders to raise concerns about ethical conduct and address, amongst other issues, improper pressure placed on valuers.

Recommendation 6 – Quality Assurance Panel
RICS should create a dedicated, independently-led valuation regulatory quality assurance panel, under the jurisdiction of the RICS Standards and Regulation Board.

Recommendation 7 – Valuation Audit Trail
The Red Book should include further standards around the conduct and recording of valuation instructions and meetings between client and valuer.

Recommendation 8 – Analytical Approaches (i) Discounted Cash Flow
The valuation profession should incorporate the use of discounted cash flow as the principal model applied in preparing property investment valuations.

Recommendation 8 – Analytical Approaches (ii) Advanced Analytics
RICS should improve the knowledge and application of valuers in respect of advanced analytical techniques.

Recommendation 9 – Global Standards
RICS should maintain a record of valuation standards adoption and application in countries outside the UK where significant numbers of its Registered Valuers operate, in order to inform the extension of regulatory requirements and support to valuers.

Recommendation 10 – Standardised Property Risk Advice
RICS should develop a framework to standardise property risk advice.

Recommendation 11 – Post-Qualification Requirements and Revalidation
RICS should review its post-qualification requirements for valuers, and consider introducing mechanisms for regular revalidation of valuers.

Recommendation 12 – Diversity
RICS should continue to build on its important work to ensure a diverse and inclusive valuation profession.

Recommendation 13 – Culture and Behaviour
There is a need for further specific RICS guidance to clarify RICS' expectations around the culture and behaviours expected of RICS professionals in the pursuance of valuation activities.

The world does not stand still, and if confidence is to be maintained, RICS, the valuation industry, and its clients must now embrace further change.

The Recommendations as a Package

I commend RICS for commissioning this transparent and independent Review, and I propose that these recommendations be considered and taken forward in full. It is my belief that implementing these recommendations as a package will lead to a greater and more enduring trust in the workings of, and ultimately the valuation outputs of, RICS Registered Valuers.

I recognise that these recommendations might not go far enough for some observers, and I volunteer that one or two of the arguments both for and against some recommendations that I might have made were quite finely balanced. Rather than approach the Review as a series of independent recommendations, I have preferred to develop these measures as a package to recognise the interlinkages between the issues, and in this way to provide a comprehensive proposal.

In example, rotation of valuers is not the sole answer to the independence question, nor to the management of conflicts; whilst declaring that valuers should be independent of multidisciplinary advisers might deal with some (though not all) of the questions regarding conflicts, it might then exclude valuers clearly capable of bringing the greatest knowledge to a particular valuation.

It is therefore the combination of recommendations that is presented here as a means of improving confidence, and it is hoped that it will be the complete package that is adopted. Picking some and not others of these recommendations would not work in my opinion. Adopting a compliance function without a fully functioning regulator with a top-notch quality assurance function would prove ineffective, as would adopting discounted cash flow as the primary valuation methodology without bolstering education of the analytical technique, nor would seeking an audit trail for meetings between valuer and client work fully without an improved cultural overlay and ethical understanding.

If the intellectual argument for these linkages and hence the concept of a package of measures is not enough persuasion, given the delicate balance I have found in judging some of these things, I suggest that it might be but a small step for a subsequent review to conclude that trust and confidence in valuers and their outputs could only be sustained if valuation services were made fully independent of wider professional services provision and/or that regulatory oversight and quality assurance should be provided independently of the profession.

It is the State that has the ultimate interest in property investment valuations, and just as we see in the medical and audit professions, for example, where the State has an overriding interest, it could be the State that provides oversight, regulation, and compliance of valuation professionals. I have concluded in this Review that this would not be the optimum solution, but the possibility remains that others might form a different opinion.

I hope therefore that the intellectual argument for the package as argued for here, and the possibility of a different conclusion in a future review, will be sufficient to encourage the energetic adoption of the changes I recommend, however challenging these recommendations might be.

I am confident that if taken as a whole and adopted robustly, these recommendations will go a long way to improving and securing society’s trust in property investment valuations.

Review Methodology

Process

In the summer of 2020, I was appointed by the RICS Standards and Regulation Board[1] to lead an independent Review into real estate investment valuations and provide evidence-backed recommendations. The purpose of these recommendations was to ensure that valuation services remain relevant and trusted. A copy of the Terms of Reference for the Review can be found in Appendix A.

To support this Review, an insight-gathering exercise was established, looking at four key themes:

- Valuation methodology
- Property risk analysis (also known as the ‘forward look’)
- Independence and objectivity
- Measuring market confidence in RICS valuer performance

As part of this insight-gathering exercise, a Call for Evidence was published, helping to gather insights on the four themes identified, between 14th December 2020 and 31st March 2021. The Call for Evidence prompted engagement across a range of respondent types, including valuers, clients, regulators, academics, and government bodies. In total:

- 182 responses were received[2]
- 63 individuals attended 8 roundtables in 7 regions

A full breakdown of the demographics, those who responded to the Call for Evidence, and those who attended a roundtable can be found in Appendices B to D.

In addition, alongside my EAG, I undertook numerous engagements and discussions with stakeholders and interested parties. We also undertook a literature review[3] to set out the context for the Review and understand how other countries, professions, and regulators have approached similar challenges. We combined this with our own knowledge and experience to inform the recommendations and observations that have been made in this Review.

It is important to note though that this Review was never intended to be an exercise in rewriting the RICS Red Book,[4] however much I have heard subsequently that this is what we have been asked to do! Rather this was always, for me, about exploring the culture and values that underpin the context for the Red Book, and the making of recommendations that could enhance its applicability and effect.

1 Details, including membership of the RICS Standards and Regulation board, can be found at: https://www.rics.org/uk/about-rics/corporate-governance/standards-regulation-board/
2 Of which 90% were from RICS members.
3 See Appendix G.
4 The current edition of RICS Red Book can be found at https://www.rics.org/uk/upholding-professional-standards/sector-standards/valuation/red-book/; note a new edition effective from 31 January 2022 is pending publication.

One of the overarching conclusions of the investigative work is that this is a deep and complex subject, much more so than perhaps the casual observer might understand. In this light, the timetable I committed to at the outset was challenging. Together with the EAG, we could not express all the nuances nor capture all the views that we heard, and we recognise that in some key instances we can only recommend that further work is undertaken. That said, I am wholly confident in the recommendations and that they provide a clear response to the challenge set by the RICS Standards and Regulation Board.

I recognise that some recommendations might not make comfortable reading for all parties to this Review, but I firmly believe that these recommendations, if adopted and taken together in the holistic package offered, will lead to a much stronger foundation for societal trust and confidence in the profession.

The Expert Advisory Group (EAG)

I have been enormously privileged to have been supported by an EAG with some of the finest minds and most respected professionals in their fields.[1] They were selected to offer a diverse insight, and they all are, or have been, leaders in their fields. This Review has been all the stronger for the breadth and depth of their opinions, their tenacity, and their preparedness to offer their time for the greater good.

All that follows in this work could not have been achieved without their considerable care, commitment, skill, and understanding. They have been stalwarts in attending meetings and assessing large quantities of information over a long period of time, and without them this work would have been far less thoughtful. I cannot thank them enough.

The output of this Review should not be viewed as the democratic result of our efforts, but everyone's views have been carefully judged in what follows. Where the reader judges that a point is well made, it should be to the credit of the EAG; where any fault is thought to lie, it should be entirely mine.

RICS

RICS is the primary institution responsible for overseeing the valuation profession in the UK and is one of the foremost property professional bodies globally. Historically, other UK professional organisations, including the Chartered Land Agents Society, the Chartered Auctioneers' and Estate Agents Institute, and the Incorporated Society of Valuers and Auctioneers, have also represented valuers but have long since merged with RICS.

With regards to valuation, RICS covers the following areas of practice:

- real estate valuation[2]

1 A full list of EAG members can be found in Appendix E.

2 Defined in the Red Book glossary as: *"Land and all things that are a natural part of the land (e.g. trees, minerals) and things that have been attached to the land (e.g. buildings and site improvements) and all permanent building attachments (e.g. mechanical and electrical plant providing services to a building), that are both below and above the ground."*

- business valuation
- plant and equipment valuation
- personal property, art, and antiques valuation

The primary focus of RICS in these areas is to set and regulate standards. It does this through ensuring that the Red Book, which sets the standards required for valuers, and all associated valuation guidance tools, which include codes of practice, professional statements and guidance notes, are kept updated. RICS upholds its standards through its regulatory activity, which includes a registration and compliance monitoring regime for valuers. It is the desire to inform the future development of this purpose that has led RICS to commission this Review.

I wish to pay tribute to RICS for the support that it has provided during this Review. I have found the RICS staff I have engaged with to be open-minded and supportive, efficient, and helpful. They have proved extremely knowledgeable, which has been an enormous help. At no point have they exerted inappropriate influence on me or on the EAG, and the work we provide here is our own, with secretarial support by RICS where required. My huge thanks go to them, for without their commitment and dedication, this work could not have been completed on such a tight timetable.

Conflicts

I am the son of a doctor with no family ties to the profession. I undertook a vocational degree in Urban Estate Surveying at Nottingham Trent in the mid-1980s and qualified as a Chartered Surveyor in 1987. Arguably I have not needed that qualification for the last 20 years; however, I maintained it and was proud to be made a Fellow in 2012. I have attended and contributed actively to the RICS and Bank of England Commercial and Residential Property Forums over the years, from where some of the preliminary thoughts for this Review arose.

I worked for Jones Lang Wootton, Drivers Jonas, and Prudential Portfolio Managers Ltd (all three names now historic, as if to prove the point made in the context for this Review below), before moving to Wellcome, where I have worked for the last 20 years, now as Managing Partner and Chief Executive Officer of the Investment Division, managing a global unconstrained multi-asset portfolio. I serve on Wellcome's Valuation and Investment Committees, where I see all manner of global asset classes and valuation methodologies.

I have both run directly, and now oversee the running of, international property investment portfolios, and at various times have engaged in depth with many of the major firms of property advisers. Some I still know well. I believe that I have a strong overall picture of the profession, whilst not being steeped in it.

In terms of formal roles held today, I am Chairman of Premier Marinas Holdings Ltd, Farmcare Ltd, and Urban&Civic Plc at the time of writing. I am on the board of many Wellcome subsidiaries and am a director of two property management companies where I have a personal interest in properties they manage; I am also a shareholder in two other small private UK property companies.

Many property firms have advised me over the years, from the very big to the very small. I report here for good order that Savills Plc currently advise Wellcome on their residential investment portfolio, Bidwells on the farmland, and Cushman and Wakefield on the commercial properties. Avison Young and CRM provide property management for Central London commercial assets.

CBRE, Cushman and Wakefield, Cluttons, Gerald Eve, Jones Lang LaSalle, and Strutt and Parker are the key valuers for Wellcome-owned direct real estate assets and operating companies at the current time.

Background

What Is a Valuation?

In my experience of property investment valuation, when the client instructs a valuation, they seek the basic measure of value, which is an assessment of the **exchange price** at which an asset would likely sell or be acquired. The client will also want suitable supporting evidence, and a rationale for the valuer's decision. The valuer and client will follow a process of agreeing terms of engagement, communicating facts, undertaking investigations, and reporting the valuation – a process set out in a brief overview in Appendix F.

Whilst a valuation is usually articulated as a single-point estimate, there is likely to be a range of estimation around this specific level. There is therefore some risk for the valuer in providing a specific valuation point estimate, and for a client in receiving and acting upon it.

Depending upon market circumstances, there will be periods of greater and lesser confidence, leading to an increase or decrease in the range of possible outcomes around the specific valuation point estimate expressed. In periods of greater risk, uncertainty, or disrupted liquidity, the range will be much wider. At such times of greater uncertainty, a deep understanding and knowledge of various valuation methodologies will assist the valuer and client greatly.

It is not the role of the valuer, as some assume, to project future performance of the asset at the valuation level (except where it would guide the valuer in predicting the likely exchange price), unless they are specifically asked to. The role of the valuer is merely to assess and explain the exchange price; it is for others to assess the **value** implied at that exchange price, and prospective future performance of that asset from that price level.

It has surprised me and my fellow EAG members that the concepts of price and value can still be confusing to some. We also noted misunderstanding of the difference between the value of an asset to the market and its value to an individual or firm (the latter being its 'worth'). It therefore seems to me that more needs to be done to underline the importance of understanding these differences, as they directly impact the role of the RICS Registered Valuer and what they are asked to do. A short glossary of terms can be found in Appendix H.

Context for This Report

I write at a time when data collection, artificial intelligence, and automated valuation techniques are gaining traction. I acknowledge that some believe the science of valuation will in time override the art. It is mine and the EAG's view that even though detailed data collection and analysis and artificial intelligence can guide the valuer increasingly accurately, especially where asset types are 'commoditised', there will always be an overarching role for the human being to provide professional judgement in assessing the inputs and outputs from a computer model.

Ultimately, I make little comment on artificial intelligence here, which is not to say that it will not gain significant followers as a feature within the valuation industry in years to come. It might in fact become preeminent, but I judge that it is not yet the answer to improving confidence in property investment valuations. I would encourage RICS to keep this developing area of practice under close review.

I note that over 25 years, the real estate advisory industry has changed significantly from a time when there were a multitude of service providers to there now being only a few major multidisciplinary practices, much as the accounting profession has witnessed. There is therefore a prima facie greater propensity for conflicts as a result of the reduced choice for clients, and we recognise this throughout the report.

Writing in the autumn of 2021, we can all appreciate the huge changes that the world is working its way through. We can see with hindsight that, in many countries, there has been a relatively benign geopolitical, macro-economic, and natural environment for well over a decade now. In such an environment, real asset valuations have increased significantly as interest rates have declined. The environment feels very different now, and not just because of Covid-19.

It is beyond the brief of this paper to discuss the relative merits of government policies that in the UK saw income streams between landlords and tenants disrupted by Covid-19 interventions, but we will recognise the pressure on future real estate income streams has never been so great. Work-from-home threatens occupational demand and rental levels; the potential depreciation of property is far more visible; and with the built environment responsible for around 40% of carbon emissions,[1] society will look increasingly to the real estate industry to play its part in the much-needed workplace and carbon revolution. Many argue that the profession is not yet doing enough. It is not difficult to predict that the exchange prices of assets that are particularly exposed to the carbon revolution will lag behind their more modern counterparts.

As leases in many markets shorten, uncertainty around rent collection, environmental, and other costs of ownership will likely rise. Therefore, the security of the income streams arising from the ownership of real estate will likely come under further pressure in the future.

Real estate increasingly needs to be seen and understood as an operating business, with the operating requirements being seen far more as the landlords' responsibility than they were in the past. The real estate industry is simply not the same today as it was in my parents' generation when long leases were the order of the day. This needs to be recognised in valuation methodologies and protocols; the role of the valuer will be no easier going forward than it has been in the past.

If this sounds concerning, it should not distract the observer from seeing real estate as an attractive long-term investment asset class, just with some similar challenges today to those of many of the other major asset classes. At the time of writing, the Cape/Shiller Price Earnings Ratio for public equities is at one of the highest points

1 This figure is widely reported by a number of independent organisations. A December 2020 UN Environment Programme article quotes 38%, including construction: https://www.unep.org/news-and-stories/press-release/building-sector-emissions-hit-record-high-low-carbon-pandemic

in its history, and in the bond markets, yields are de minimis, though rising, as the hypothesis that inflation is more than transitory starts to take hold. I expect that particular debate will take a while to conclude (I note that property has hedging characteristics that not all the other major asset classes share), but for those who argue that these markets today are priced too highly, I suggest that the risk premium for well-located, well-managed, and well-valued property should remain and provide both defence and opportunity for investors with a long-term horizon.

Real estate is a real and long-term asset, and gains much of its attraction from its ability to weather economic storms and provide utility, security, and financial returns over time. That should remain true, even whilst the nature of leases changes and both operational responsibilities and costs increase. Whilst the ownership of real estate remains compartmentalised, economic rent should still travel over time to the ultimate owner, and the economic growth generated by a society should eventually end up in land and real estate values.[1] That process might not be smooth, but well-positioned property should still make for a good long-term investment for institutions and society's participants, in my opinion.

History clearly indicates however that there is a 'property cycle', and I encourage the reader and valuers of property to become thoroughly acquainted with that. It is beyond my terms of reference here to discuss this, but I consider it one of the most important features of developed property market behaviours and should be mandatory reading for aspiring property investors. I write at a time when I firmly believe we are in the second phase of what historically has been an 18 to 19-year cycle in developed markets.[2]

If this proves to be correct, the next few years will yet confound those who argue the direction of real estate prices is downward from their elevated position today. Such a possibility provides an opportunity for us all to get our houses in order before an eventual correction besets us. If the cycle does not hold, and the shorter-term outlook is more difficult, this might be all the more reason to act with urgency today.

It is my hope that the recommendations here might therefore come just at the right time for the profession to adjust its valuation practices ahead of what will at some point become a more challenging period.

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1 See David Ricardo's theory of rent.

2 See:

Fred Harrison, *The Power in the Land* (1983).

Richard Barras, 'Property and the economic cycle: Building cycles revisited'. *Journal of Property Research*, 1994.

Philip J Anderson, *The Secret Life of Real Estate and Banking: How It Moves and Why* (2008).

Findings and Recommendations

The Terms of Reference[1] identified four initial themes to consider; this Review makes findings in respect of each of these.

During the course of the Review, it became clear to me that it was important to document my wider findings. Some of the observations I have made developed from the initial questions asked during the insight-gathering process, and have led me to what I believe will be the most important of the recommendations that I make in this Review.

I would therefore like to highlight at the outset that this Review has expanded beyond the initial enquiries in the Call for Evidence, though I trust the Review is now more complete for this. It is also worth noting that while this Review is global in nature, due to the locality of the working groups and respondents to the Call for Evidence, it is largely focused on the UK market.

In total, I, with the support of my EAG, make 13 recommendations. These constitute the principal areas in which I believe RICS should focus its attention. Whilst I hope the RICS Standards and Regulation Board takes note of all the recommendations, for me there are three recommendations that are the most pivotal. These are:

i. The creation of a dedicated, independently-led valuation regulatory quality assurance panel, under the jurisdiction of the RICS Standards and Regulation Board.

ii. The creation of a formal Valuation Compliance Officer role within regulated valuation providers to ensure services are delivered appropriately, objectively and to the standards observed across today's financial services industry. This role is envisioned to provide a robust foundation for full accountability and responsibility of valuation firms to their clients and to the valuation regulatory quality assurance panel, particularly where multidisciplinary services are provided to clients.

iii. The need for further specific RICS guidance to clarify RICS' expectations around the culture and behaviours expected of RICS professionals in the pursuance of valuation activities.

I set out more information on the findings and recommendations below.

Conflicts of Interest

One of the first issues that quickly arises when discussing independence and objectivity is conflicts of interest. Valuation by nature involves the interaction of different parties with specific interests, which can inevitably lead to conflicts. The effective identification and management of these conflicts of interest is therefore a challenging but essential part of being a professional valuer. However, as I have observed throughout my career and heard throughout the process of this Review, conflicts of interest still exist in the industry, and there is a question around what more can be done to resolve and lessen the adverse impact of these conflicts.

1 Terms of Reference are included in Appendix A.

The RICS' Red Book and *Conflicts of interest* professional statement[1] clearly identify that unmanaged conflicts of interest are unacceptable. I do not find fault with these standards but believe that their application can and needs to be bolstered, as it is essential for society that valuers can demonstrate independence and a lack of conflict at the time of undertaking their valuations.

It is clear to me that the definition of independence today is not absolute, and several examples of embedded conflicts were provided during the Review that in my opinion would seriously test the patience of the layman. Some were really quite surprising in this day and age. One such example, whilst not widespread, was of valuation fees being quoted in relation to the change in value of the asset over time. Another more common example of a potential conflict lies in the length of time that a valuation firm and/or individual valuer can hold valuation instructions for a particular client. Some surprisingly long periods were quoted in evidence for this Review.

Not all conflicts lie with the valuer. Clients instructing valuations when they are individually rewarded directly on the outcome of those valuations is a clear yet widespread example. Those clients are conflicted, and this should be recognised and managed well by those that oversee them.

I also note there is a close association between valuer independence and conflicts of interest (and I elaborate further on valuer independence in the next section). Some areas of practice require particular scrutiny and management of potential conflicts, including in my experience the practice of an agent's firm acting in the purchase of a property being given the subsequent valuation instruction post-purchase. I note that Sir Bryan Carsberg in his review almost 20 years ago (noted in Appendix G) identified similar themes; not all of his recommendations seem to me to have been adopted in full.

This need for effective management of conflicts is particularly true in the case of the higher-risk valuation purposes related to public confidence matters identified at the outset of this Review.

Similarly, I consider that the concept of 'informed consent' (where a conflict is acknowledged but accepted) is useful in principle but requires strict management in practice, as its application can be fraught with challenges. I am aware from discussions with major industry stakeholders that application of informed consent is not uniform. It is therefore important that clients understand the nuances; a mere declaration of conflicts existing does not necessarily absolve them.

It is therefore important that RICS works to strengthen understanding among valuers and their clients of how they can apply RICS' requirements, as set out in its *Rules of Conduct* and its *Conflicts of interest* professional statement, which is paramount in this situation.

I note and have been guided by the requirements of the UK Takeover Panel in association with the Takeover Code,[2] which governs public market transactions,

1 RICS' *Conflicts of interest* professional statement can be found here: https://www.rics.org/uk/upholding-professional-standards/standards-of-conduct/conflicts-of-interest/

2 The Takeover Code can be found here: https://www.thetakeoverpanel.org.uk/the-code/download-code

and I believe that RICS should develop standards based upon and around those same principles to ensure that the principle that a conflict is not extinguished through declaration alone is properly embedded into the culture and actions of the profession. I note that the Takeover Panel requires very wide consideration of where a conflict might lie, far broader than would be standard today in the matter of property valuations. For reference, a summary of the Takeover Code is included in the literature review in Appendix G.

Recommendations

Recommendation 1 – Commissioning and receiving valuation reports
RICS should work with appropriate stakeholders in standardising governance arrangements for commissioning and receiving valuation reports for high-risk and 'regulated' valuations.

In addition to the recommendation set out above, RICS should also continue to develop its conflicts of interest guidance and standards for practitioners, and to assist clients with instructions. When setting out the standards, I would propose that the metrics applied to the assessment of conflicts of interest should be 'absolute', as they cannot be seen to be 'negotiable' at the point of instruction. Similarly, valuation fees should also be set in absolute terms, independent of an index or the value of the asset, or the change in asset value over time.

I would also suggest that a valuation firm's Valuation Compliance Officer (see Recommendation 4) should confirm the firm's ability to act without conflict. Where clients are also Chartered Surveyors, the conflicts of interest policy should apply to them as robustly as it does to the Registered Valuers providing the valuations. Similarly, when valuations are required in 'high-risk' situations or for 'regulated' valuations (as stated – where share prices or unit prices are derived from valuations), I feel strongly that the valuation report should be instructed by and submitted to the Independent Chair of the Audit Committee of the client or its equivalent.

I also strongly encourage the practice that the valuers hold independent meetings with the non-executive directors or their equivalent. Where regulated valuations are being undertaken, I would also like to see a summary of the valuation instructions published alongside the outputs, although I recognise that this is in the hands of clients and beyond the terms of this Review.

Valuer Independence and Rotation

The topic of valuer independence was one of the most notable of the discussions I had with the EAG, and frankly proved one of the knottiest of the challenges that we faced. Many contributors brought anecdotes of varying levels of concern. It was always clear that this was going to be an important topic if confidence in valuations is to be restored and maintained. Combined with the 'conflicts' points addressed above, I describe it as one of two major 'elephants in the room' that we uncovered in our investigative work.

No one coming into this Review, even before it had formally started, failed to recognise that the decision of the UK accountancy profession's regulator, the

Financial Reporting Council (FRC), to request the separation of audit from advisory services by 2024 creates a crucial precedent for our own deliberations.

I am aware of the disquiet amongst clients and the general public that ultimately led to the separation decision, and the disruption that this is allegedly causing within the profession during the process of separation. I note anecdotal suggestions of increased fees for audit services now being borne by clients, and in some instances disruption in the services provided, but it is difficult to ignore such an important precedent.

On this issue, I therefore took wide soundings both formally and informally. On the one hand, there is the view, quite reasonably, that valuation should only be undertaken by those entirely independent of any function or wider activities within valuers' firms. On the other hand, many valuers claimed that their ability to do their job well was because of their direct access to their market-facing colleagues. This is also quite reasonable; the argument being that to provide an up-to-the-minute valuation requires up-to-the-minute knowledge of rents and prices being paid, as well as who is in the market.

It is clear that the close relationships that develop between valuers and their clients can be an important jigsaw puzzle piece in the positioning of the multidisciplinary practice as the provider of other advisory services to the client. Independent valuation service providers argue that this can 'cloud' the output.

The EAG noted that the argument for maintaining a valuation function within a multidisciplinary practice was made most strongly by those within those big multidisciplinary practices. The point was not lost on the EAG that on the limited occasions when valuation cases do come to court, it is often the smaller and fully independent valuation experts that are appointed to advise the parties.

I had expected to find the weight of the arguments above well balanced, and I do. The accountancy profession tilted me toward believing a recommendation to separate valuation and advisory services might be the right way to go. Ultimately however, on the balance of the evidence, I have come down on the side of maintaining the status quo, because I believe that it results in potentially better outputs for the client and hence society. However, I add one essential recommendation (the need for a Valuation Compliance Officer in those firms) for this conclusion to be effective, and this is discussed in my findings and recommendation section below.

In addition to the arguments made for whether there should be a separate valuation and advisory service, it was interesting to note that many of the responses to the Call for Evidence highlighted that rotation was a key aspect for improving confidence in the profession, and that guidelines in this area need further consideration and/or to be made mandatory. For example, one valuer suggested that *"enforced rotation of valuers is a controversial topic but should be considered openly and fairly"*, and a response from a large professional services firm suggested that:

> *"rotation is key to maintaining valuer independence and safeguarding against 'familiarity' threats to valuer objectivity. Firm rotation should be mandatory and brought into line with the audit profession."*

The findings from the Call for Evidence responses strongly suggested that the requirements around rotation of valuers were currently not clear enough or strict enough. It was noted for instance that in the Red Book there is a *“good practice, albeit not mandatory”* recommendation *“to rotate valuers at intervals not exceeding seven years”*. In this Review, I agree that this does not go far enough.

The EAG and I discussed at length the experience of other professions in respect of rotation, particularly audit. The recent (2018) Kingman independent review of the audit profession suggested that the regulator (the FRC) had not been *“as effective as it might have been in shaping the debate on major issues related to its work, such as … auditor rotation, or on the relationship between audit and non-audit work”*. The regulatory system for audit has further developed policy around rotation and separation of functions since. I do not find audit to be a perfect analogy for the situation in valuation as I set out below, but I do recognise that rotation and interaction of multiple disciplines is an issue where there is the provision of a number of professional services.

To bolster the requirements included in the Red Book, I think it is necessary to comment on a suitable period for rotation. The UK Statutory Audit Services Market Study (2019) is noted with interest, stating that:

> *“the current requirement on public interest entities is to carry out an audit tender at least every ten years, change audit firm at least every twenty, and for the audit firm to change the lead partner every five years. The BEIS Select Committee recommended revisiting this, moving to a fixed term of seven years.”*

We also noted the comments in the roundtables around rotation periods, including the following suggestion:

> *“in Europe, there is growing momentum for mandatory rotation of valuers every 3 years or every third instruction. The EBA’s guidance on this is best practice, not mandatory.”*

Recommendations

The topic of independence and conflicts is fraught with difficulty in unregulated and private markets, where transactions are typically founded upon the bargaining power of the parties. Independence is critical to establishing trust in the output of a valuation process, as is the perception for wider society that those outputs are ‘unconflicted’.

The ‘easy’ answer might have been to recommend the independence of the valuation professional from their advisory colleagues; however, this runs the risk of poorer outputs overall, and I therefore recommend other mechanisms in the short term to counter the accusations that currently bedevil the industry.

I recognise the strength of the argument that valuation must be separated from other services, and that this would provide the only true unencumbered view of value, but I find myself more sympathetic to those who argue they have access to the data and the flow, which enables the valuations to ultimately be more reflective of the market at a point in time than an independent at risk of not having all that information. I also have personal experience of that. It is not therefore quite the same as the issue that was faced by the accountants.

Whilst this conclusion will be a huge relief to some and deeply frustrate others, it is most certainly not to be seen by the reader as a decision that leads to 'no change'. Indeed, the recommendations that follow may be viewed by some as considerable change in process and protocol, and I judge will come to be seen by many as being fully as demanding as a recommendation of separation – especially those asked to enact them if they are accepted.

To support the position I reach here, it is important for the integrity of the valuation profession that client information, data sources, and instructions are secure, both from external and internal leakage. RICS should work with valuers to ensure that the same level of confidentiality is applied to data and instructions as is expected in all other parts of the valuation process, and that this forms part of a robust governance framework.

Recommendation 2 – Valuation and Advisory Activities
Valuers, with the support of RICS, should ensure that the separation of valuation from advisory activities within firms is consistently applied in respect of the use of valuation data and instructions.

One of the ways of solving this valuer independence question is to recommend a regular rotation of valuers. This itself is a double-edged sword. The rotation of valuers places a high burden on both clients and valuers alike, and I judge that rotation in itself would not necessarily lead to better outcomes. It can however help with perception, and for this reason it stands here as a helpful tool in our armoury.

I make a clear distinction between private organisations or individuals seeking valuations where third parties might not be directly reliant upon those valuations, and where valuations are provided for regulated purposes (as described previously, where unit or share price transactions might occur as a result of the valuations), for example in publicly-listed property companies and in property unit trusts.

I fully appreciate the burden that comes with a recommendation to rotate valuers, both for valuer and client alike. However, it seems to me that if one is not to seek separation of valuers from multidisciplinary practices, it is essential to recommend rotation to ensure relationships do not become too cosy. This is especially necessary when valuations are undertaken for regulated purposes, where society has an interest.

I therefore distinguish between the two distinct types of clients in coming to the recommendation. As a guideline I would suggest the maximum term of an appointment of a valuation firm by any client is 9 years, reduced to 5 years if it is in the category of potentially higher-risk valuation involving collective third-party reliance.

Recommendation 3 – Rotation
RICS should develop a time-specific, mandatory procurement and rotation process for valuers.

If we are to accept a valuer might work within a multidisciplinary practice, and must rotate, I consider there is one further step required to complete a fully robust recommendation on this matter of independence and conflicts. The EAG and I therefore make a further critical recommendation in this regard, having observed the workings of other financial service advisers and institutions.

Compliance

Issues around independence and objectivity can often be resolved through strong standards and regulation, and compliance with them. Compliance is therefore integral to the risk management function across professional services companies – including those closely linked to real estate valuation such as financial, audit, and legal services.

Compliance has enhanced the quality of service provision for consumers. Looked at through the lens of the property investment valuation industry, it might be expected that valuation firms would have a specific valuation compliance function, similar to those that are found in other professional service industries such as the financial services industry. Such functions clearly benefit the firms, their clients, and consumers alike; however, I have found that this is not the case with property valuations.

Looking at other industries, the role of a Compliance Officer is crucial to making sure that the company (including that of a sole practitioner) is conducting its business in full compliance with all national and international laws and regulations that pertain to a particular industry, as well as adopting fully professional business practices and ethical standards as they would be understood by clients and the public.

The insight I have gathered from other industries suggests that the compliance role, done well, involves striking the right balance between the legal, ethical, and pragmatic requirements of meeting regulatory requirements. The role is crucial in helping organisations manage risk, maintain a positive reputation, and ultimately avoid lawsuits.

Discussions with key stakeholders in the market have emphasised the broad role of the Compliance Officer to me. They are responsible not just for maintaining a company's business dealings but also for educating the entire company and ensuring institutional-grade practices of the highest order. Compliance Officers are therefore an essential component of corporate behaviour and governance, and they usually report to the board of the company they work for.

The essential quality of a Compliance Officer is that they are ethical and principled, with a strong conviction for doing what is right and willing to take the lead on corporate integrity.

Recommendations

The EAG noted that in many instances the client, especially where regulated valuations are being undertaken, will have their own compliance function. I believe that it would be highly beneficial for the valuation firm providing services to such a client to have similar accountability and responsibility.

Whilst the Compliance Officer is an essential component in financial services companies, I note that the property industry has not, until recently, embraced the role in its own practices around property investment valuation. I believe that the disciplines that would come from a compliance function done well within firms of valuers, multidisciplinary and sole practitioner alike, would considerably enhance society's confidence in property investment valuations.

A compliance function would particularly fulfil the need for full accountability and responsibility to be taken by valuation firms where multidisciplinary services are provided to clients, and would ensure services are delivered appropriately and to the standards observed across other regulated industries.

Clearly, I envision the formal Valuation Compliance Officer role in firms of valuers to be a senior appointment, similar to those in the Senior Managers and Certification Regime under the UK Financial Conduct Authority. Put more bluntly, the role must have 'teeth' and report at main board/partnership level.

It seems to me that there is conceptually an opportunity here in the governance structures of valuation firms to also involve lay persons or non-executive directors in their oversight and governance of valuation services, but I do not feel that I should make this a formal recommendation. It seems to me that clients will naturally migrate over time to those valuers that offer the strongest governance of their own affairs, and this development will evolve of its own accord if the practice is thought valuable.

For the sake of clarity, I consider that the Valuation Compliance Officer role would be different from, but complementary to, a 'responsible principal' within an RICS-regulated firm, in that the role would be specifically responsible for reviewing compliance with valuation standards. It would also go beyond the Compliance Officer role set out in the Red Book, which currently only applies where potential conflicts of interest have been identified.

Recommendation 4 – Compliance Role
RICS should build on its existing 'RICS responsible principal' obligation by developing a Valuation Compliance Officer role to specifically cover valuation process and conduct.

Accountability and Oversight

If independence, objectivity, and a reduction in actual and perceived conflicts is the first major plank of recommendations made in this Review, the second must be the topic of accountability and oversight. Notwithstanding the excellent job that most valuers do, and recognising that their job is very difficult, particularly during times of change or market stress, there needs to be both a market perception and demonstration of appropriate oversight and accountability to create the level of trust we seek.

Oversight of professionals is of critical importance to society, whichever the profession and whatever the competence. In the matter of property investment valuations, where the results when aggregated pose a potential systemic risk to society, it is essential that there is, and is seen to be, strong regulatory oversight for professionals and firms undertaking this work.

The advantages of there being a regulator and standard setter such as RICS for the property profession are manifold. A key component of this role is the ability to maintain governance and ethical standards, and key drivers of success are the ability to provide a route to raise concerns about ethical practices within regulated activities and to provide quality assurance to the wider world.

The topic of oversight and accountability of valuers, and how these might be optimised, arose regularly in our deliberations and proved another of the most challenging questions that we faced.

RICS leads one of the great professions with a Royal Charter, of which it should be rightly proud. At a time of challenge to professions generally, and to those with a Royal Charter especially as to their role in society, it seems to me that it is imperative RICS continues to invest in and strengthen its role as an assurer and regulator of professional competence and conduct.

Confidence in society comes from knowledge that appropriate oversight is in place, as well as witnessing a job done well by a competent person. The level of confidence in valuations is therefore dependent upon the quality of the oversight of the valuation process, as well as the quality of the work undertaken.

On the one hand, I am fully satisfied that the RICS Standards and Regulation Board is a body with its heart and motives in the right place, and that it seeks to do an excellent job of providing standards, support, and regulatory assurance, both for its membership at large and specifically for RICS Registered Valuers. On the other hand, I received consistent feedback that whilst the process for engaging with valuers about the quality of their work and the levels of governance employed was probably appropriate for a time of long leases and secure income streams, it would now benefit from being refreshed and strengthened in order to maintain quality in today's fast-changing world.

It is clear from our discussions with the wider valuation fraternity that most RICS Registered Valuers recognise the benefit of regulation and a robust regulatory function, and they believe that RICS is best placed to deliver this, rather than regulation by a separate party. The minority however struck the greatest chord with me and the EAG, arguing that, at a minimum, current quality assurance protocols should be enhanced and that an independently-led quality assurance panel, dedicated to valuation, was a prerequisite of enhanced accountability.

I think it is also important to look beyond the valuation profession to try and find much-needed answers to the important questions around accountability and oversight this Review raises. Although not a medical professional myself, my personal and professional connection with that sector means I have watched its regulatory development with interest. I admire the reformist zeal shown by Sir Donald Irvine in chairing the General Medical Council (GMC) from 1995-2002 and promoting its reform from the outside, both before and afterwards. I admired his focus on service quality and the need for checks on professional competence, including revalidation.

I note with interest that challenges around self-regulation are ones that the GMC and other medical professions wrestle with to this day, including the need for the independence and the perspective of external (lay) contributors to any effective regulatory oversight system. I recognise that RICS has taken important steps, having introduced lay-majority regulatory governance in 2007, and further strengthened this in 2020 with the creation of the Standards and Regulation Board, but I think valuation is a special case within the wider family of surveying services because of the risks explored and explained throughout this Review.

In 2004, Sir David Clementi's review of legal services examined the oversight of professional bodies in the legal services sector. Whilst this, and the subsequent Legal Services Act in 2007, did not lead to a formal separation of the professional body and the regulator, it did lead to significant changes in governance and control. Sir Donald and Sir David were ahead of their time, but they forged a path for me to follow in this Review.

Recommendations

I could not, in the time available, lift every stone on the question of external versus self-regulation in the property investment valuation industry. We know that it is a critically important topic, and it requires deep and careful consideration. Some guidance however might be helpful as I set a path of recommendations for RICS to follow.

It is of course the very essence of being a professional that one holds to standards above and beyond those of wider society, and that one is accountable to one's professional body for the holding of those standards.

RICS is the leading professional membership body for real estate in the UK and has a major role in real estate markets globally, operating for the public advantage under its Royal Charter. Its remit encompasses a wide range of important functions, including regulation, standards, education, thought leadership, and advocacy. I am aware that some observers would instinctively question whether such a span can house effective regulation.

My own considered opinion on this point is that RICS, with its deep understanding of the profession and the environment within which its members operate, should be the natural provider of regulatory oversight for all of its professional members. It should therefore be best placed to deliver optimum outcomes, so long as it maintains a steadfast independence in its regulatory governance and operations, and ensures the necessary investment in people and systems to achieve robust quality assurance for the highest-risk areas of practice.

RICS' professional members are registered across a range of sectors globally. Some 16,000 of these are RICS Registered Valuers. Currently, all RICS members are regulated by the RICS Regulation team. An important part of this regulation and any oversight mechanism is that there is a route to raise concerns about ethical practices within regulated activities. This helps RICS regulate, and also helps ensure the public's trust and confidence in the profession is maintained. The mechanisms for raising concerns therefore need to be clear in order to ensure this is effective, which is how I arrived at my next recommendation.

Recommendation 5 – Raising Concerns
RICS should ensure it has clearly signposted processes for its regulated members and other stakeholders to raise concerns about ethical conduct and address, amongst other issues, improper pressure placed on valuers.

As I have noted already, it is to RICS' credit that it has already set up an independent governance board, the RICS Standards and Regulation Board, to which this Review is reporting. This board is independently led by a lay Chair and has a majority of lay members, and it is delegated sole responsibility for RICS' public interest functions (RICS qualifications, entry to the profession, standard setting, regulation, and dispute resolution).

Having reflected carefully upon the role of the Registered Valuer within the wider membership of RICS, it is mine and the EAG's judgement that the addition of a more focused, bespoke, and specific valuation regulatory quality assurance panel would be appropriate in order to help the RICS Standards and Regulation Board ensure the best possible regulatory quality assurance regime for property investment valuers, given the ultimate potential for systemic risk to society.

I especially note here the role and function of the UK Takeover Panel in mergers and acquisitions in public markets. Here we have a highly respected small group of experts overseeing the functioning of highly visible and potentially contentious activity within public markets. The Takeover Panel oversees the application of the Takeover Code and ensures compliance with the Code *"through a consensual approach with the parties engaged in takeover activity"*.

There is a clear read across from the RICS Red Book coverage of valuation governance to the Takeover Code; however, there is not the equivalent specialist function within RICS to provide the sophisticated level of focused assurance advice offered by the Takeover Panel. Ultimately, of course the issues between valuer and client should not prove as sensitive as those between a bidder and their target; however, I can see the need on occasion, especially for high-risk valuations, for very high-quality advice and guidance ultimately underpinned by the powers that RICS already has to direct appropriate actions by RICS members.

Examples of where such guidance would be helpful would be where valuers and clients seek assistance on conflicts of interest and process, and where clients and valuers alike seek guidance on ethical practice. It should not be the intention that a valuation oversight function would make a judgement on the appropriateness of a valuation itself; rather, it should observe on the methodology and process by which a valuation has been determined.

The Takeover Panel has statutory powers (derived from the Companies Act 2006) to direct bidder and target entity as to how to behave, and ultimately determine what is acceptable and what is not. Failure to adhere to due process and conflict requirements risks criminal sanction. As someone who has held the role of a Registered Person under the Code, one does not sign up lightly. So it should be for the valuer, particularly where they conduct valuations for regulated purposes.

I note that valuation services that are for performance measurement which provides a forward look may be regulated by other parties in addition to RICS. I note that RICS does not have similar statutory powers to the Takeover Panel. Its current regulatory powers are extensive; however, I recommend that RICS considers carefully whether they are sufficient to deliver the sort of quality assurance regime that I describe here.

It seems to me that the Standards and Regulation Board of the RICS, an existing structure within the RICS ‘family’ yet independent of RICS’ Governing Council and with lay members, could host a valuation assurance function that could operate very effectively. I therefore envisage a dedicated team, of the same nature as the Takeover Panel, sitting within the independent oversight umbrella of the RICS Standards and Regulation Board. It should have similar directive powers to determine, for example, whether a firm could undertake a valuation or whether a process had been followed.

I note the responsibilities of the FRC, which is an independent regulator with a public interest mandate, as they promote transparency and integrity in business. The FRC regulates auditors, accountants, and actuaries and sets the UK’s Corporate Governance and Stewardship Codes. Their work is aimed at investors and others who rely upon company reports, audit, and high-quality risk management. Amongst their powers, they can and do undertake spot audits. The RICS also holds this power, though I have uncovered in my research that there is a feeling it could be used more effectively.

I believe that an independently-led valuation regulatory quality assurance panel, with lay members, reporting to the Standards and Regulation Board should be able to meet modern-day requirements of independence and expertise, and give RICS what it needs to deliver a ‘best-in-class’ regulatory function for valuation.

It will be for the RICS Standards and Regulation Board to debate the powers that they should have to make such a panel fully effective. The analogy with the medical profession is the General Medical Council (GMC), which has legal powers through the Medical Act 1983. Medical revalidation is therefore underpinned by law. The Takeover Panel similarly takes it authority from the law through the Companies Acts.

Whilst one would hope that the main function of the valuation regulatory quality panel would not be to sanction potentially erring practitioners, it would need such capabilities to be fully effective. I would hope to see such a panel able to ensure that practitioners could not practice until they have, for example, completed a performance review or received any necessary education, and that they are reassessed subsequently. For the most serious faults, further sanctions should be available.

The RICS Charter and Byelaws allow the Standards and Regulation Board to make rules about the use of disciplinary powers. The Regulatory Tribunal Rules, as they are now known, set out the processes, decisions, and regulatory actions available. It seems to me that the RICS Standards and Regulation Board therefore has the powers to consider the question of discipline or sanction for RICS Registered Valuers and RICS members involved in valuations if need be. I would envision that the powers held by the Standards and Regulation Board would flow through to the valuation regulatory quality assurance panel to take forward its responsibilities effectively.

Recommendation 6 – Quality Assurance Panel
RICS should create a dedicated, independently-led valuation regulatory quality assurance panel, under the jurisdiction of the RICS Standards and Regulation Board.

Detail on a valuation regulatory quality assurance panel

A dedicated oversight group of the type envisaged in the recommendation above would also have the role of providing quality assessment and quality assurance. Quality assessment describes the monitoring and appraisal of valuations against predetermined standards and principles. Quality assurance goes one step further, requiring action to be taken on any deficiencies revealed through quality assessment.

Quality assurance is an essential component of good management and technical practice, both of which are substantially interdependent. The provision of a good service will not of itself assure quality (though it is a good start). In relatively complex organisations involving many people and modern practices, there needs to be the resources in terms of people, time, money, and skill to translate the general notion of quality into structures, policies, systems, and results.

An expanded facility for bespoke valuation quality assurance and advice to be provided by RICS would undoubtedly contribute to personal professional competence and development. Property investment valuations require significant skill, professionalism, care, and knowledge, and the provision of an optimum service for clients is dependent upon the individual and the firm's ability to provide each of these together in a well-structured format.

A valuation regulatory quality assurance panel under the jurisdiction of the (independent) RICS Standards and Regulation Board would be able to, for example, aggregate some of the insight it receives whilst working with industry to prepare high-quality 'state of the market' valuation reports. These reports would compare valuations with market data on transactions in reports that have been well received by the industry and observers alike in the past. An example of this type of research is the Valuation and sale price insight previously undertaken by RICS, further details of which are included in the literature review in Appendix G.

A valuation regulatory quality assurance panel would also be able to commission and/or sponsor academic research into advanced valuation methods with a view to providing guidance to the profession, including worked examples.

There are three preconditions for quality:

i. Access

ii. Money

iii. Confidentiality

A specialist valuation regulatory quality assurance panel should be empowered to assess quality right across the valuation spectrum. It should therefore be able to access the valuers and their clients, and those valuers and clients must have absolute confidence in the behaviours of the assurance team.

The second precondition is money. Quality normally costs money, and in this instance it will. The notion of value for money will be a legitimate objective, but quality is much more likely to be achieved and protected if the service being provided has access to suitable supporting resources. I recognise that the recommendations here may lead to resourcing challenges, especially in the context of RICS' global role and the differential maturity of valuation practice in many countries today.

However, it is important that a suitable budget for a valuation regulatory quality assurance panel (or other such appropriate name) is made available by RICS to the Standards and Regulation Board. It is not for me to suggest how this initiative be delivered, but I would hope that a reallocation of resources from within the organisation might be the appropriate way forward. It is noted that the Takeover Panel works with secondees to great effect.

The basic terms of reference for RICS' proposed valuation regulatory quality assurance panel will be to gather information, analyse the data, identify patterns and behaviours, interpret and understand the findings, advise on corrective actions, and monitor and report on subsequent performance where remedial action is recommended. The qualities that will contribute to successful performance monitoring will be appropriate leadership, organisation, technical ability, culture, and the ability to influence behaviour.

Quality assessment and quality assurance involve complex concepts and will be difficult to manage in practice. This should not lead RICS to the conclusion that it is too difficult. With the right vision and leadership, I consider that this is fully achievable and desirable.

The Red Book

The Red Book sets out the standards to which RICS valuation professionals must adhere. It incorporates the common, global concepts defined in the International Valuation Standards (developed by the International Valuation Standards Council) and aims to provide an effective, regulatable framework for delivery of these standards to clients. Given its importance to the valuation profession, it is right that I examine whether the level of detail and mandatory requirements are right – particularly in relation to independence and objectivity, which is an issue that has arisen throughout this Review.

It was a particular concern that one professor of valuation (someone I hold in the highest regard) suggested in one of our first meetings that the Red Book market value basis of value might not be fully fit for purpose in valuations for lending purposes.

The consensus among the responses to the Call for Evidence suggested that the profession believes the current RICS Red Book requirements in respect of valuer independence are considered sufficient.

However, there was also an acceptance among the respondents that the practical reality of applying the standards comes with difficulties. For instance, a question was asked in the Call for Evidence as to whether there were any other material threats to valuation objectivity. The answer was an unequivocal yes, with *"client pressure"* being frequently referenced. Comments were often strongly worded, with one commentator attending a review roundtable stating that *"the pressure from clients is completely unacceptable and totally unprofessional. So there is client reform needed as well as valuer reform."*

This suggests to me that there is more that could be done to make the Red Book requirements in respect of conflicts and independence stronger and more explicit. This should be in addition to the recommendations external to the Red Book made above, for example those relating to signposting routes to raise concerns.

Recommendations

The EAG and I heard evidence that, in the main, the Red Book was a solid and sensible document providing substantive directions for appropriate behaviour and procedure, and was to be commended. We noted that it has been updated regularly over the years and we commend RICS for that.

I do not consider that it was the role of the Review to look in detail at individual line items in the Red Book, but one matter in particular arose as it relates to independence and accountability (also dealt with above). It is mine and the EAG's view that requirements in respect of conflicts and independence should be made more explicit.

It was noted that the current Red Book is a daunting document, especially for clients, and that the reader might benefit from its structure being simplified to make it more accessible.

As part of the Review process, the EAG and I heard concerning evidence of the pressure that can sometimes be placed upon valuers by clients to alter draft valuations. This is clearly acceptable where facts need to be clarified, but we recognise the risk of something beyond 'fact checking' occurring, and the anecdotal allegations in some quarters that valuations are *"merely a negotiation between the valuer and their client"* are alarming.

The Red Book currently contains detailed commentary around the potential for conflicts where valuations are discussed with clients before completion. I would like this to be extended, made firmer, and be better applied by members.

While most of the accounts we received were anecdotal and cannot be supported by evidence, we sadly gained a sense that 'misbehaviour' is occurring unchecked in some quarters. This is not to say that it is widespread, but it undermines confidence in the whole valuation process, however professional most valuers and clients appear to be. Sadly, only a few rotten apples can spoil a whole batch, and I therefore regrettably advise that the standards and guidance of the RICS Red Book should be written for the lowest common denominator, not the highest. This finding led me to my next recommendation.

Recommendation 7 – Valuation Audit Trail
The Red Book should include further standards around the conduct and recording of valuation instructions and meetings between client and valuer.

I propose that where valuations are undertaken for regulated purposes, client instructions for valuations should be made available to the valuation regulatory quality assurance panel where appropriate.

In order to achieve this, I suggest that meetings between valuer and regulated purposes client should be monitored, minuted, and recorded. Recordings, minutes, and other notes of valuation meetings between client and valuer should then be available for compliance and governance checks by clients through Valuation Compliance Officers, non-executive directors, or their equivalent, as well as internal and external auditors. For example, it is the practice at Wellcome Trust that meetings between the property team and the valuers also involve the Head of Risk and the finance team, including our external auditors when appropriate. Such meetings need to be subject to confidentiality and any third-party regulatory governance procedures.

It is my view that clients requiring valuations for private purposes should adhere to these protocols, but whilst it will represent 'best practice', Recommendation 7 above need not be mandatory.

Valuation Methodology

The insight gathering done by myself and the EAG brought home the range of purposes for which investment valuation is undertaken globally, and the range of different valuation methods used. Each method can of course produce a different result, and in certain situations more than one method may need to be used as a cross-check.

The required balance between principles and prescription is neatly captured in the Call for Evidence responses. However, whichever camp one sits in on that discussion, unless valuation is totally prescribed, different methods, techniques, and inputs can naturally create inconsistencies in valuations, even when undertaken for the same reason.

It struck me through our insight gathering that clients are becoming increasingly discerning about how valuation outcomes are arrived at, and they are becoming increasingly critical of the methodology used. This is particularly the case as the property market is now more analytical than it was in the past, and clients expect that there should be more transparency in the data points used. This suggests more prescription is potentially needed.

Equally however, prescriptive standards may not be suitable to cover the vast range of valuation circumstances and I judge could lead to unwarranted valuation conclusions in some situations. It might also not be appropriate in less-developed global markets. What is apparent is that clients are becoming less accepting of 'implicit' valuation inputs, assumptions, and outcomes within the method and models used; instead, the models should be 'explicit' to achieve the required levels of transparency, understanding, and education.

The Call for Evidence consultation asked how prescriptive RICS should be on the application of valuation methodologies and models. Whilst many respondents were clear that increased prescription was not necessary in most cases, one frequently commented upon area where standards and guidance might usefully be required was in respect of discounted cash flow (DCF) models.

For example, one valuer confirmed that they are *“adopting a greater use of DCFs across the UK business as a response to market requirements and to mirror how market participants are increasingly pricing assets”*, with another suggesting that *“RICS should issue clear guidelines on preferred methodologies to be adopted and increasingly recommend DCF as the primary methodology for all income-producing real estate.”*

Comments also came from the client side, an example being from an asset manager who suggested that *“use of DCF is to be encouraged”*, but who warned *“the more variables that are introduced to the valuation without robust evidence for their prevalence, the greater the potential for volatility.”*

I acknowledge that work has also been considered previously in this area, as set out in the Mallinson report on commercial property valuations (RICS, 1994). The report covered methodology in detail and made the following recommendations:

> *“RICS to develop a common professional standard for the all-risk yield methodology and work on ‘codifying and disciplining’ discounted cash flow (DCF) techniques”.*

The responses and discussions in respect of this Review suggest that the discounted cash flow methodology has become increasingly important and suitable for modern markets, and that guidance on the use of discounted cash flow would be welcomed, including RICS recommending that it should now become the primary model for undertaking property investment valuations.

I will admit that it has been something of a concern for me that some valuations I have received over the years cannot be fully rationalised mathematically. For example, a valuer might discount a let residential or agricultural property from its vacant possession value by a ‘rule of thumb’ amount, yet if one mathematically assesses that assumption, it does not always accord with actual rents paid and time that might be taken to realise vacant possession. The capital markets’ use of adjusting price expectations in 25 basis point steps might be another example.

I have seen several examples in my own career of valuations not quite keeping pace with property development situations where value accrues over time, for example through the gaining of a planning consent or during building works. I recognise the difficulty of such situations for the valuer but feel that traditional valuation practice runs the risk of not fully capturing exchange price in such circumstances.

It seems to me that the discounted cash flow methodology, with appropriate scenario analysis, might well lead the valuer to conclude that the exchange price could reflect some of the future value a little earlier, whilst recognising that if the consent was not forthcoming, the valuation might fall back.

Discounted cash flow with explicit inputs might also help in the challenging matter of valuing structured real estate investments. A 50% share in a £100 asset is not necessarily worth £50, and minority interests often trade at discounts to reflect an illiquidity and possible lack of control in the interest that does not necessarily manifest itself at the asset level. I can certainly think of the opposite being true too. It is well beyond the remit of this paper to explore such phenomena, but the requirement to think explicitly about the required rate of return might well lead the valuer to consider these things carefully going forward.

In one final example of the benefit of using the discounted cash flow methodology going forward, it seems to me that it might far better capture the reality that property is now being seen as an operating business. The discounted cash flow methodology opens up the possibility of recognising more transparently that a property asset in the hands of one operator might have a different prospective return outcome than in the hands of another. With an understanding of the possibilities, greater certainty might be placed on the valuation. This being said, there are challenges (identified above) around the difference between the market value assessment of operational real estate and its worth to an individual operator. This review is concerned with real estate value and not the value of individual businesses, but I note that where there is a greater understanding of the worth of a property investment to a particular operator or operators, a greater appreciation of the likely exchange price for that asset might also be gained.

In each of the examples given, and others I could think of, the discounted cash flow methodology might enhance clarity and understanding, and would hopefully result in a more robust valuation.

It was also notable from the Call for Evidence responses that views differed globally around the issue of valuation method prescription. There was clear support for prescription in valuation from developing economies, and a suggestion of targeting guidance and support for these regions – particularly around circumstances where traditionally low levels of market activity meant resorting to, for example, cost-based valuation approaches.

Similarly, the Call for Evidence highlighted the differences around the world that need to be recognised and considered, particularly in training and guidance around the methodologies, and in how the profession should deal with the variety of markets and approaches to valuation.

For instance, as a valuer highlighted in their response:

> *"additional guidance and training are always very useful. But once again, training based on European or US standards, rules, laws, and regulations are not very useful for valuers in other countries that have totally different socio/ social-economic, geographical, and even meteorological circumstances, e.g. the Caribbean, India, Latin America."*

Another respondent valuer wished for RICS to expand *"beyond a focus on the United Kingdom/European region"*. Others were positive about the work RICS was doing globally, such as a participant in one of our roundtable insights gathering sessions who put forward that *"in Saudi Arabia, RICS is making a difference and more locals are becoming members, which means more trust is created in the region."*

Recommendations

The EAG and I have considered the evidence from the profession and have drawn upon our knowledge and understanding of valuation practices across a wide variety of asset classes, especially where there is no recognised investment exchange providing price discovery.

One particular benefit to the valuation process might be where there are listed real estate markets that can provide a degree of price discovery. Listed real estate markets provide a lens on both the equities and property markets, and whilst they should not be blindly followed, to ignore them completely seems equally inappropriate.

As an investment practitioner who firmly believes there is much useful information in markets beyond the one in question (for example, that bond markets can provide information on tenant credit quality), I find it a little concerning that property market investment valuation practice has tended to limit its observations to direct property comparables.

That said, I also note that we now have, in the majority of circumstances, valuers of investment properties utilising a DCF methodology for their valuations, if only as a check on their traditional methodologies. I find this commendable and would like to see the guidance to do so strengthened.

I acknowledge that traditional measures of value, such as an 'all-risks yield' calculation, can correctly identify the exchange price at which an asset will likely trade (the all-risks yield is merely the mathematical summary of the many assumptions that go into a valuation), but the use of the all-risks yield does not provide sufficient information and clarity to the client on the make-up of the value of their property. In circumstances where a traditional income capitalisation approach is the most suitable method, the valuer should justify this in their analysis and reporting, and provide appropriate written commentary that gives support to their conclusions on the yield adopted and the valuation result.

I therefore strongly prefer the use of explicit discounted cash flows to assess the likely exchange price that a property would command in the open market. Such cash flows should account for matters such as the prospective growth rate (net of depreciation), the risk premium, and the discount rate for the derived cash flows; the discussion with the client should be all the richer for this.

Recommendation 8 – Analytical Approaches (i) Discounted Cash Flow
The valuation profession should incorporate the use of discounted cash flow as the principal model applied in preparing property investment valuations.

Recommendation 8 – Analytical Approaches (ii) Advanced Analytics
RICS should improve the knowledge and application of valuers in respect of advanced analytical techniques.

The EAG and I noted that the profession in the UK responded consistently to state that RICS should not interfere in the choice of valuation methodology. Many UK valuers were of the view that the methodology should be a matter for their judgement and expertise, based on the valuation circumstances and evidence. However, the EAG and I similarly noted that international correspondents felt that greater guidance could be provided. I therefore think that more can be done to consider different valuation requirements globally.

Recommendation 9 – Global Standards
RICS should maintain a record of valuation standards adoption and application in countries outside the UK where significant numbers of its Registered Valuers operate, in order to inform the extension of regulatory requirements and support to valuers.

Property Risk Advice

The majority of methods used in valuations have a common trait: they all use comparative, available data to produce a current valuation as the basis of value agreed with the client, and this is often perceived to be backward-looking. Clients are increasingly asking for the long-term future value or a property risk analysis, and valuation methodologies can also be used to create a more forward-looking assessment (most notably the income approach or investment method).

Valuers can be reluctant to engage in discussions around a property risk analysis and the forward look because it can be seen as more of a prediction than a valuation. It is therefore naturally riskier for the valuer than assessing current market value and raises liability concerns. The point is also not lost on me that valuation is often a regulated activity, whilst the provision of strategic advice and other forms of investment consultancy might not be.

There was a lot of feedback from the insight-gathering process on this. One of the elements that struck me was that there is still some confusion between property risk advice and valuation. There was a clear view from members and other stakeholders that more could be done to assist clients in understanding how to instruct valuers in any additional supporting requirements they might have. Similarly, there was a clear direction from the responses to the Call for Evidence that RICS plays a vital role in ensuring this understanding through engagement with the profession and clients, and by providing guidance and advice.

Whilst the evidence clearly showed an appetite for further guidance on property risk advice, it was interesting that respondents to the Call for Evidence were split as to whether advice around property risk could be provided by valuers.

There was particular concern about providing calculations of worth. Some saw this as a part of the valuer's remit whilst others did not, or they believed that such advice would need to be heavily caveated. For instance, a valuer from a large valuation advisory firm suggested that *"property risk analysis is appropriate advice to sit alongside an assessment of fair/market value."* Furthermore, such advice *"could significantly elevate the profile of what we can really deliver for the benefit of clients' future evolving requirements."* However, an investment manager commented that *"advice concerning future investment worth would constitute a material expansion in the role of the valuer."* Similarly, a different valuer commented that *"we don't feel we should be advising on investment worth, as this is subjective to the individual client."*

In addition to discussions on whether it was outside of the remit of the valuer or not, an academic respondent suggested that *"most valuers do not have the ability to perform quantitative analysis on risks and their impact on investment worth."* This was reiterated by a government property professional who questioned whether the valuer has *"the personal tools (skills, ability) to properly undertake forward-looking quantitative analysis"* and suggested that *"given the lack of strong focus on this in the past, many perhaps do not."*

Discussions and responses to the insight-gathering process also highlighted that it is not just whether the valuer has the skills, but whether more can be done to ensure clients understand how to instruct a supporting risk analysis. In the Call for Evidence, I specifically asked whether more can be done to ensure clients understand this. It was interesting to note that most respondents from all sectors agreed that it can.

Many suggested RICS could, for example, develop a risk template to assist in this area, something that I believe RICS should consider. A contributor to one of our review roundtables commented that:

> *"as markets continue to develop and advance, and as clients' needs continue to grow in terms of sophistication, additional demands are being placed on valuers to provide advice involving some element of prediction or forecast. Great care is needed to ensure that such advice is not misunderstood or misrepresented, and that any sensitivity analysis is carefully presented so as not to undermine the basis of value adopted."*

The question around whether more can be done to instruct a supporting risk analysis also exposed the potential problem of liabilities around property risk advice. One valuer suggested in their Call for Evidence response that:

> *"the reservations many valuers may have relate to potential professional indemnity insurance implications. Separation of such supplementary risk analysis within the terms of reference would potentially address such concerns, with a clear acknowledgment that this additional risk analysis is separate to an independent external valuation and should not carry the same liability as an independent external valuation."*

Similarly, there were several references made in the Call for Evidence and roundtable sessions to the need to deliver better instructions for property risk advice.

One commentator in professional service simply suggested that property risk *"is a training need"*. A lender respondent commented that *"examples of best-in-class conveyed through CPD will help the professional as a whole"*. This should feed into the wider thinking that is explored in this Review on education and training.

Recommendations

As highlighted above, the EAG and I received a number of submissions on the topic of the ‘forward look’ or property risk advice, which is not the same as an RICS Red Book valuation and it should not be described as such.

I believe that RICS should provide further guidance to the profession on the matter of the forward look or property risk analysis. This guidance should ensure that the fundamental technical differences between price and worth, and a valuation and a forecast, are well understood.

The EAG and I note that the techniques valuers are well trained in to assess the current exchange price of an asset should not in themselves be considered an adequate platform to forecast future exchange prices. I wish to make clear that, whilst undertaking a property investment valuation in a strict sense may only require limited knowledge of the interaction of real estate markets, financial markets, and the wider economy, a forecast of prospective performance requires far more extensive knowledge.

As recommended elsewhere, property risk advice should be founded upon the discounted cash flow methodology, the proper use of which will require appropriate skills.

It is not obvious to the EAG and I at the current time that valuers should provide this advice to clients alongside a valuation report (though we note that they are often asked to do so) in the absence of a change in their education and training – which we recommend elsewhere in this Review.

I believe that property risk advice should always be provided in a separate report to that of a valuation undertaken in accordance with the Red Book, even if instructed at the same time and undertaken by the same professional or firm.

I further recommend that fees for valuations and for property risk advice are kept separate to avoid confusion about what is being paid for and where responsibilities and accountabilities lie, and the wording of the appointment letter should be able to deal with this.

Recommendation 10 – Standardised Property Risk Advice
RICS should develop a framework to standardise property risk advice.

One particular area of property risk, or forward look, that arose during our discussions was the topic of sustainability and climate risk. The EAG and I recognise this to be a substantial topic for the industry and we recommend separate work is undertaken for the benefit of the profession as a whole, in order to help assess the impact on the future performance of property.

This Review does not, as some might expect, deal in detail with such recommendations. This is not to make light of this critical subject.

Valuers are required to assess the exchange price at which an asset would trade in the market, having assessed relevant market comparables, risk premiums, depreciation, and growth rates. Ultimately however, as has been described elsewhere in this Review, it is not the role of the valuer to provide a judgement on whether this is the right price or not. Rather, the valuer must assess the exchange price, which will take account of all the issues that the market will consider in what it would pay for an asset.

Sustainability and climate change will be major factors in that consideration, but if, for example, a valuer felt that the market was taking insufficient account of the impact of climate change on an asset, it would still be correct for the valuer to assess the exchange price based upon the valuer's knowledge of the market's pricing. Of course, should there be an instruction alongside the valuation to assess the future performance of the asset, it would be expected the assessor would focus heavily on the subject and highlight where their concerns lay.

Training and Ongoing Education

I recognise that RICS is currently undertaking an education review, and many of the topics that were raised in this Review are general requirements for all surveyors. However, given the specific importance of training and ongoing education to the valuation profession, I feel it right to emphasise and include training and education in this Review.

The profession is currently well-recognised for its requirement for relevant qualifications and the need for ongoing development. This is critical to maintaining trust and confidence in the valuation profession. However, while the need for training, qualification, and ongoing education is recognised, it is important that it is the right training, qualification, and ongoing development.

It is crucial that education maintains pace with market conditions and demand because without this, trust and confidence from all stakeholders might be lost. It is essential those that undertake the complex process of valuing land and the buildings that sit upon it are appropriately qualified to do so.

This Review explored this important topic and the EAG and I note that there has been a reduction in face-to-face teaching in universities over time. This leads to a reasonable challenge from the educators that there is currently insufficient time to teach the deeper aspects of property investment valuation, such as advanced mathematics and data analysis, and their application. Clearly this could lead to a loss of faith in the capabilities of those moving into the valuation profession.

In a world that now offers cryptocurrencies, complex securities, and derivatives, with professional compliance and regulation, the days of a valuer relying upon an 'all-risks yield' should be numbered. Education must be the building block upon which such a shift must occur.

A high level of technical competence is a prerequisite for improved performance but is insufficient on its own. In a fast-paced world, technical competence can wane over time and must be refreshed. Clients should be entitled to know that those who were competent in the past are still so today, and valuers should be entitled to look to their professional body for the ongoing educational opportunities that they require.

During the insight-gathering process for this Review, it became clear that there was a lot of support and enthusiasm for continuing professional development (CPD). The responses I received to the Call for Evidence specifically highlighted the importance that the valuation profession and others place on CPD and more training. For instance, one valuer from a large multidisciplinary firm stated in their response to the Call for Evidence that:

> *"arguably it should be mandatory for members to undertake additional training in order to ensure and maintain high-quality valuation and safeguard public trust and confidence."*

Feedback from the insight-gathering process also highlighted that there is a need to introduce specified CPD requirements for the valuation profession, and a need to review whether 20 unspecified hours annually (with no requirement for valuation-specific content) provides appropriate and sufficient learning and development for registered valuers. One respondent to the Call for Evidence highlighted this by suggesting that:

> *"the Valuer Registration scheme should be updated with a focus on valuation-specific training as part of annual CPD requirements, and RICS audits should have more focus on methodologies and making sure the valuer has the right skills."*

Recommendations

From the evidence the EAG and I have reviewed, I firmly believe it to be critical that RICS further enhances the skillsets of the Chartered Surveyor via specialist and dedicated training for those who choose to take the route of becoming a Registered Valuer.

I suggest that Registered Valuers should be subject to dedicated CPD requirements to support continuous improvement over the years they are in practice. I am aware of the review the RICS Education and Qualification team is undertaking, and I ask that the reviewers there consider the evidence from this Review when looking at post-qualification requirements and possible revalidation.

It is my view that there should be a suitable period for revalidation of a valuer's skills and competencies, and hence their fitness to practice, particularly where working in high-risk and complex areas of valuation. My view is that a constructive form of revalidation should occur at suitably regular intervals, and should be appropriate to the type of work being undertaken.

Recognising the sensitivity of this recommendation, I still suggest that it is an essential ingredient in the building of societal trust in valuations. I suggest however that the exact approach, including the period of revalidation, should be a matter for further detailed consideration. From the perspective of this Review, which focuses on upholding confidence in property investment valuations across society, I would guide the RICS Education and Qualification review towards a revalidation cycle of not more than 5 years.

I will watch with close attention the outcome of the education review, and in the interim make the following recommendation to the RICS Standards and Regulation Board.

Recommendation 11 – Post-Qualification Requirements and Revalidation
RICS should review its post-qualification requirements for valuers, and consider introducing mechanisms for regular revalidation of valuers.

Diversity and Culture

As for most things in life, property investment valuation should not be a ‘mostly male’ industry.

I have spent some 35 years working in and around this profession, and recognising my own stereotype (white, middle-aged, male) I find it a sad reflection that the profession is not more diverse and balanced at the current time.

One notable feature of the Wellcome Trust investment team, throughout the time I have worked for it, has been that we have sought to be ahead of the curve on issues of gender balance, diversity, and inclusion, and I believe that this has been a substantial advantage and a contributing factor in our strong performance over the years. I’m proud of the work my organisation continues to undertake in this area.

It is my heartfelt desire to see a far greater balance of diversity, inclusion, and equity in the property profession. In my judgement, the profession would be so much richer for it, and consequently so would society. Market forces will determine the speed with which the societal changes that we are witnessing today will be embraced in the property investment valuation arena, but I hope that this work will accelerate that change.

As part of the analysis for this Review, I also considered the work of other organisations, and it was noteworthy that organisations such as the Financial Reporting Council comment on areas such as diversity and inclusion in their annual trend reports. While this Review did not specifically focus on diversity and culture, it was telling that only 3% of respondents were APC candidates. While I infer that they are likely to be younger, I had hoped that more would have felt able or willing to respond.

We did not explicitly capture the gender split of those replying; however, I fear that the number of female respondents was similarly low. That said, one of the most thought-provoking of our respondents, with a powerful story to tell, was a senior woman in the valuation profession. This, along with my own experiences, suggests that there is much more that can be done to ensure greater diversity and inclusion across the profession, and particularly in the valuation arena.

Recommendations

The EAG recommends that the RICS Standards and Regulation Board takes strong steps to improve the diversity, equity, and inclusion mix across RICS membership, with particular emphasis on attracting a diverse group of Registered Valuers to its membership in order to enhance the standing of this element of the profession.

Recommendation 12 – Diversity
RICS should continue to build on its important work to ensure a diverse and inclusive valuation profession.

Much can be said about the importance of culture in all aspects of society, and we will not reinvent the wheel here. That said, there is one key aspect that the EAG raised as part of its review of confidence in property investment valuations: the industry is exposed to, and some would say rife with, the potential for conflicts of interest – something I have gone into in detail above.

The EAG and I recommend that the RICS Standards and Regulation Board release a document for the valuation profession detailing the standards of behaviour that are expected of Registered Valuers in particular, and the profession as a whole. I would recommend this contain a series of worked examples for professionals to reflect upon and take guidance from. It should not be characterised as a list of 'must do' rules and requirements.

Ideally, this future work would serve as a benchmark text for how to think through and handle common examples of the challenges encountered in everyday working practice.

I have in mind guidance akin to *Good medical practice*, produced by the General Medical Council, last updated in March 2013 and issued to every practising doctor in the UK. Clearly RICS would make such adjustments to some of the principles therein as they deem appropriate.

Recommendation 13 – Culture and Behaviour
There is a need for further specific RICS guidance to clarify RICS' expectations around the culture and behaviours expected of RICS professionals in the pursuance of valuation activities.

Other Issues Arising from the Review

One important issue that arose during the course of this Review was the lack of adequate, appropriate, and affordable professional indemnity insurance (PII) for valuation professionals, which incorporates the wider issues of risk, reward, and liability.

PII is one of the most significant issues facing firms and Chartered Surveyors today, and whilst not formally within the scope of this Review, I encourage RICS to continue to work with partners and external stakeholders in the insurance market, and carefully consider the outcome of the current RICS review of PII requirements in the UK. Ultimately, I can see a real risk that fewer and fewer firms of valuers will be available to the market to undertake valuations in the future. Whilst this might be good for those few firms that can afford the premiums, such an outcome would reduce competition, increase the potential for conflicts, and work against some of the recommendations of this Review.

I therefore encourage RICS to address the serious and valid concerns of both insurers and valuers, and provide solutions that enhance the confidence clients and society can take in the property investment valuation process.

Another issue worth commenting on here is in respect of valuation and market indices. Evidence gathered for this Review indicated that there was a general lack of understanding of how real estate value indices are constructed and their appropriate uses.

I recognise that these indices have a valid function in the market and that RICS does not have jurisdiction over their production or use. However, in light of their market influence, I would suggest RICS opens a dialogue with the providers of prominent indices to explore how to promote a better understanding of them and their appropriate uses.

Another issue that I make no specific recommendation on but is of note, and which is impacting on both valuers and Chartered Surveyors more broadly, is that of sustainability and environmental social governance (ESG).

The EAG and I are of the view that the valuation profession and its stakeholders should work together to better understand the impact of these factors on valuation, and how best to equip valuers to tackle these issues in the future.

Recommendations 8 and 10 above focus on sophisticated valuation and property risk measurement methods and are recognised as being particularly important to the assessment of ESG-relevant factors, as is the commentary above related to property risk. It is my view that RICS should take a strong leadership position in addressing this area through education, training, and the publication of supporting guidance.

Ultimately, a valuation must reflect the valuer’s best estimate of the exchange price at which an asset will trade, and sustainability and ESG factors relating to that property will be inherent in that valuation as the market digests these factors. It is not the role of the valuer to guide the profession, but to make accurate observation of likely exchange prices. It is RICS that needs to guide the profession on property risk, and it should be expected that market participants will incorporate the guidance into their buying and selling activities.

During the course of this Review, I also note that some correspondents shared with me anecdotal examples of other real estate industry practices, particularly around capital market transactions. I felt that these examples clearly fall outside of the valuation remit that I was given in undertaking this Review. However, I have acknowledged these and will be recommending to RICS that these practices might form worthy topics for further consideration, given the involvement of RICS members in some cases.

Conclusions

There have been several significant matters that the EAG and I have had to consider in our Independent Review of Real Estate Investment Valuations for the RICS Standards and Regulation Board in 2021, a year in which the world faced huge challenges arising from the global Covid-19 pandemic and in which we have been unable to meet face to face.

These challenges included the vexed questions of whether, to name just a few:

- valuers can ever be considered ‘independent’ if they are a part of a wider multidisciplinary practice offering other advisory services
- the valuation industry (valuers and clients alike) takes conflicts of interest seriously enough
- the RICS Red Book provides sufficient guidance to valuers
- valuers should be forced to revalidate and rotate regularly
- greater guidance on valuation methodology should be provided

Over and above the main ‘essay questions’ that we initially explored as part of the insight-gathering process we have also had to consider a number of further material issues arising from the evidence gathered.

In this category, the evidence highlighted the need for further questions to be asked about oversight, quality assurance, and the role of compliance as essential tools in the critical role of maintaining society’s trust in property investment valuations. Additionally, we considered the challenge of continuing to educate valuers to the level of competence required and considered whether valuers should revalidate their skills regularly.

I have met with many participants in our Review, albeit virtually due to constraints in the period during which I undertook this work. I am most grateful to them for their time and contribution. I have listened to all and have weighed all their contributions carefully, from the most articulate to the least, and from the most inexperienced to the most experienced. I have been both pleasantly surprised on the one hand and saddened by other anecdotes that have been shared, but I am confident that the EAG and I have formed a good understanding of the issues at hand.

Whilst we have learned a huge amount, I fear that for all that learning, there may still be areas that we have not fully got to the bottom of. For example, I have not in the time available had a chance to understand the difficult issues around UK professional indemnity insurance (subject to an RICS review at the time of writing), nor do I comment in detail on sustainability as a function of the ‘forward look’ as I would have liked to have done. These will make fruitful topics for future reviews or working parties.

Notwithstanding that I committed to a timetable for this Review that with hindsight has proven challenging, I have set out a series of recommendations in which I have confidence, and that I believe would seriously advance a sense of well-being and confidence in property investment valuations on the part of society.

Whilst I make several detailed recommendations, there are two central and key matters that I believe need to be addressed to underpin confidence in property investment valuations.

The first is that I believe that trust in property investment valuations will only be materially enhanced across society where there is the perception of robust independent regulatory quality assurance for the valuation profession. I have therefore recommended that RICS creates a valuation regulatory quality assurance panel, under the oversight of the independent RICS Standards and Regulation Board, to help it strengthen its regulatory functions in this most critical of areas.

A successful quality assurance programme should be comprehensive and should address both the organisational and technical aspects of property investment valuations. It should also be systematic and planned, and whilst I consider it essential that the panel is ultimately independent of RICS' Governing Council, I recommend that it should be developed with the full cooperation of RICS itself, valuers, clients, and other stakeholders.

The valuation regulatory quality assurance panel should concentrate on, and expect to find, areas for improvement across the spectrum of activities it oversees. It should present to the industry areas for improvement mainly through incentives and encouragement but be able to recommend corrective measures as a long stop if necessary. It should cultivate a high level of confidence amongst participants and ensure a high level of confidentiality.

Where quality assurance, coupled with a programme of standards and guidance, is done well, it can help explain the services of valuers and the role of property investment valuations to the wider society.

There would be one further potentially significant benefit. A valuation regulatory quality assurance panel as described in this Review would prove a robust defence to those who would (as some do) argue that fully external assessment and control is the optimum regulatory model in this circumstance. It is a valid question, and was asked by Donald Irvine over 20 years ago of the medical profession: *"In my diary I questioned more than I had ever done before whether professional self-regulation as we know it was really viable."* In this Review, I have rejected the notion that it is not viable in the property profession, but in so doing I observe that RICS must maintain relentless attention to strengthening oversight and assurance around property investment valuations to ensure they remain fit for purpose in a fast-changing world.

The presence of the independent Standards and Regulation Board in the governance structure of RICS has enabled me to make what I consider to be an optimum recommendation: that the new valuation regulatory quality assurance panel can sit under its jurisdiction, with its own regulatory powers.

This is not a compromise. Had there been no established independent body within the RICS governance structure to which the valuation regulatory quality assurance panel could report, and which would have the public interest at the forefront of its mind, I might have looked again to Donald Irvine's musings that perhaps it would be necessary to create a fully independent quality assurance function from which society could seek comfort, with all the consequences for the profession that this might have entailed.

If this comes as a relief to RICS, I suggest that this should not be viewed as an 'easy' recommendation to action, but it is one with a significant prize if it can be implemented effectively. If it cannot be performed under the jurisdiction of the Standards and Regulation Board, I judge it would likely need to be subsumed into the remit of another body, and without the committed involvement of RICS and its members I fear that it might not be done so well.

The second core topic that proved both complex and quite tricky to unpick was the issue of valuer independence and conflict management. I find that both must be managed better by the profession to sustain the level of belief and trust required to support confidence in valuation outputs.

I regularly heard that valuers should be independent, and be seen to be independent, particularly of capital market functions; conflicts of interest must be taken more seriously; valuers should rotate regularly; education and the building of valuation skillsets are critical to the competence of valuers; and valuers should be required to revalidate regularly.

I answer these critical questions in the recommendations above and observe in so doing that the management and maintenance of conflicts, of education, and of quality are all usually handled by the compliance and risk functions in the major financial services firms today. I conclude that the property investment valuation industry should essentially be no different, given that there is ultimately a systemic risk in valuations. My second overarching recommendation is therefore that the critical role of compliance needs to be taken seriously by valuers, and that in so doing, many of these important questions and challenges can be addressed.

The Valuation Compliance Officer, whose role could be seen to derive from the workings of the 1986 Act, should in the future work with their colleagues in the firm to enhance working practices and provide a channel for accountability to clients for the services and the manner in which they are provided. I recommend the Valuation Compliance Officer function becomes the point of contact for the accountability of the firm and its services through their engagement with RICS' valuation regulatory quality assurance panel. The Valuation Compliance Officer function is in my view essential.

Taken together, the combination of a 'top-down' oversight and regulatory function delivered through an independent valuation regulatory quality assurance panel, and the 'bottom-up' accountability that comes from an effective compliance and risk management mindset within each valuation practice, should secure trust and confidence in the valuation profession.

It will therefore be critical to the underpinning of confidence in property investment valuations that the interface between the regulatory function of a fully effective quality assurance panel overseeing, guiding, and liaising with the well-run compliance and risk-oriented valuation firm be done exceptionally well. There is much precedent for this across financial services firms and regulators, and I encourage the Standards and Regulation Board and RICS to consult widely across these other industry sectors to design and then implement a second-to-none regulatory and compliance regime.

Whilst these two recommendations stand out, I recognise that it is no small matter to also guide the valuer and client to the use of discounted cash flow as the primary valuation methodology; to improve the digestibility of the Red Book and the frameworks and procedures around commissioning and receiving valuations; to argue for regular rotation and revalidation of valuers; to separate valuation services from advisory functions, when often provided by the same multidisciplinary practice; and for clients to demand improved practices around the giving and recording of instructions and meetings, including the greater involvement of non-executives where possible.

All of this needs to be overlaid by guidance from RICS on the standards and ethical behaviours that should be expected of a Registered Valuer (and the client where that client is also an RICS member, as is often the case) acting as a member of a profession with a Royal Charter.

Taken all together, I hope that this proves a comprehensive series of recommendations that will create a firm foundation for confidence in property investment valuations going forward.

Closing Comments

At times of change, it is usually recommended to move swiftly towards the new normal. Human beings however tend to prefer stability rather than change. *"Humankind cannot bear very much reality"*, as TS Elliott is often quoted as saying.

It is therefore often the case that there can be a delay in enacting change. The argument for delay is usually that great care needs to be taken to avoid making a strategic error; the argument in favour of speed is that acting swiftly might head off what might otherwise prove even greater change being required in the future.

I have long wondered whether the UK property industry's exemption from the jurisdiction of the Financial Services Act 1986 (the year in which I started my career) would prove something of a pyrrhic victory for the industry.

I wondered back then, at the beginning of my career, whether if property came under the jurisdiction of the 1986 Act, the industry might have equal standing with the other major asset classes. I reflect again on that today, now towards the end of my career. It was not a straightforward question to answer then, and it is not now. We can however always learn from the past, and we now have another chance to build upon society's improved understanding of best practice in governance, oversight, regulation, and valuation methodology.

My EAG colleagues and I are struck by the need for the profession as a whole to modernise its practices, and to do so quickly. We are also aware that our Review is being undertaken alongside other reviews of great importance to RICS. It is our heartfelt desire that the other reviews that are being undertaken at the same time and the consequences of those reviews will not prove a hindrance to the consideration of the important recommendations we make in our Review.

This Review arose because warning signs around behaviour and practice have been observed in and around the profession. If there are insufficient changes to current ways of working, all of the key actors will certainly find an even more critical situation ahead. In that sense, I encourage the reader to see this Review as something of a wake-up call for the industry and to see the opportunity that this Review and its recommendations provides: that of creating a strong foundation for behavioural change in professional practice, upon which the profession can build.

There are to my mind significant challenges here for all parties: for the Standards and Regulation Board in enabling a critical, respected valuation regulatory quality assurance panel capable of sustaining public trust; for valuers in understanding and rising to the challenge of altered working practices, embracing discounted cash flow as their primary valuation methodology (with all the education requirements that will need to go with that), placing far greater attention on conflicts and their management, and practising in a culture fully aware of compliance and risk management; and for clients in altering their working practices and recognising they must take their fair share of responsibility for the position that the valuation profession finds itself in today.

Truth, it is said, often comes out in the end, and through this Review we lay some of that truth bare for all to see. That said, whilst I found some current practices to be concerning and make recommendations to alter those going forward, I have also found many examples of very high-quality professionals striving to do an excellent job, for which they should rightly be proud. I am particularly grateful for the honesty shown by many of those professionals and companies toward this Review in calling out where change is required. I trust the outputs of this Review are their sufficient reward.

There are many reasons to believe that if these recommendations are adopted, the real estate profession, overseen by the RICS Standards and Regulation Board and with the supporting commitment of RICS, with engaged clients and valuers alike, will continue to lead the world.

The EAG and I held several global meetings, and we were struck by the different stages of development in different regions. Ultimately, we opted to make recommendations for the highest denominator, hoping that best practice will cascade down under RICS guidance to those less developed today, but I recognise that this will largely be seen as a UK-focused Review, biased toward commercial property valuations. It is my sincere hope that the practices and recommendations made in this Review will over time find themselves reflected in practices involving all real estate valuations globally. The proud history of RICS in leading global standards gives me much hope in this regard.

As always, the stronger actors will survive, adapt, and advance. The opportunity to adapt valuation practices and ways of working is here for all of us.

It is clearly my hope that the outputs from this Review will be well received, but I am realistic enough to know that elements will not go down well in all circles. I am under no illusions that my recommendations are demanding and require careful thought, from RICS especially. I hope for an energetic response, but some of these recommendations will take time to develop into well-formed new practices, and RICS should be given sufficient time to enact these recommendations thoughtfully if they choose to do so. I would encourage regular review of progress by the SRB so that some of the more demanding of these recommendations do not get lost.

I will close by restating my thanks for the opportunity to consider such important matters as property investment valuation practice around the world and offer one final thought about incentives. Charlie Munger is one of the most famous and enduring investors in the world as the trusted partner to Warren Buffett at Berkshire Hathaway. Charlie is known for his many wise statements, and the one that comes to mind here is *“show me the incentives; I will show you the actions”*.

There are significant positive and negative incentives at play here. The EAG and I are quite clear about the opportunities and the threats that this Review reveals. I hope that RICS and the industry see these similarly and respond accordingly. Whether the positive reasons for change appeal more to the reader than the fear of the negative consequences of not changing should not matter. Both incentives point us toward changing our actions today. I hope that the case has been well made, notwithstanding the challenges.

Whether readers think it is right or wrong that the valuation profession should be facing challenges today does not matter. There is currently a perception that the valuation process could be improved and does not always lead to an appropriate conclusion. The perception should be enough in itself to mean this Review has been worthwhile.

What matters now is not to debate these perceptions (we have done that here), but that the profession as a whole now steps up to support the valuer in the critically important role they fulfil in society by providing appropriate protocols, guidance, and crucial oversight. The valuer must do their bit and raise their game through the effective use of controls, compliance, and a risk management culture, and so must the client, for they are also part of the picture that has developed over the years.

If all the parties addressed here can adopt their respective 'top-down' and/or 'bottom-up' recommendations, and can effectively do what is now required, each will refine the other as they develop, and we should create a virtuous circle of improvement for this critical societal issue.

I certainly hope so.

I believe in this profession. I believe in RICS, and I believe in the role of the RICS Registered Valuer in providing essential and respected information to clients and for society.

Property is important to all of us, for it is the social and financial fabric upon which our society stands. It is my sincere hope that this Review, with its series of interlinked recommendations, will in due course greatly enhance the standing and the role of the property profession in our society, the RICS as a relevant and effective global professional members association holding a Royal Charter, the RICS Registered property valuation firms and individual valuers as experts and leaders in their field, and real estate owners and managers as they oversee the property that is the very fabric of our society.

Peter J. Pereira Gray

December 2021

Appendix A – Terms of Reference for the Review

Overall Aim of the Review

To make recommendations to RICS (and other relevant bodies) in respect of real estate investment valuations, which will ensure services remain relevant and trusted.

Context, Issues, and Drivers

RICS is the leading global professional body for property valuation service providers, with 16,000 registered, regulated professional valuers. Valuations produced by RICS-regulated members underpin financial reporting and decision making for trillions of pounds' worth of land and real estate assets in the UK and globally.

In the UK, RICS is the only substantial professional body and regulator of this professional service, although this position is not established in statute.

An estimated 70% of global wealth is held in land and property assets. Ultimately, much of global bank lending is secured upon these land and property assets and their use in business scenarios. For this reason, valuation plays a critical role in supporting overall market confidence and economic stability. As the leading professional body in this area, operating under a public interest charter, it is essential that trust is maintained in RICS' standards and protocols.

RICS applies valuation standards through the Red Book, which provides the core mandatory and advisory guidance for regulated individuals and firms providing valuation services. The Red Book incorporates the high-level principles and definitions of the International Valuation Standards (IVS), and applies additional RICS requirements and guidance, acting as a one-stop regulatory framework for professional valuers.

Over the last year, RICS has received extensive market feedback (principally, but not solely, from the UK) that valuations of investment portfolios for financial performance reporting purposes risk being considered not fit for purpose. Criticism has centred on valuers' ability to keep pace with market realities such as:

- Rapidly evolving investor and occupier demand.
- Changing occupational trends and their impacts on investment in real estate (e.g. online retail, lease lengths).
- Institutional real estate investment becoming more widely understood to be an actively managed business activity, where the management ability has a material impact on worth/value.
- The suspension of UK property funds at perceived market turning points.

This criticism has been combined in some quarters with concerns over the independence of valuers from their clients when reporting on investment performance.

These questions and others are being asked in the context of changing public expectations about the independence of professionals (especially statutory audit), so there is a need to ensure that RICS' standards and protocols are robust enough to withstand public scrutiny.

For this reason, the independent Standards and Regulation Board of RICS has agreed that an external review is necessary at this time to provide evidence-backed recommendations on these issues. RICS considers this review to be of critical importance to the profession's future, and the findings will shape its future regulatory strategy.

Parameters of the Review

- This review will focus on all aspects of valuations of property assets for investment purposes, including sustainability.
- Evidence gathering sessions will be held in all key RICS markets involved in valuations of property assets for investment purposes.
- The Review does not extend to the RICS monitoring and enforcement model; however, recommendations may need to be transposed into the model in due course.

Specific Areas for Consideration in Phase One

Valuation Methodology

- Should RICS be more prescriptive in the requirements it places on members to employ certain valuation approaches, methodologies and techniques in particular circumstances?
- Would any increase in prescription on methodology lead to a reduced obligation on the professional valuer to reflect a particular market characteristic?
- Do the current applications of valuation methodologies meet market requirements, i.e. do valuations provide sufficient information to clients and others who rely on them about the factors that have influenced the valuation opinion?
- Do the requirements of the Red Book/IVS create an adequate global/national framework for provision of high-quality valuation advice?
- Is there a need for additional guidance, training and data for RICS valuers to support the provision of high-quality valuation advice?
- Can professional valuers make better use of technology to deliver high-quality valuations?

Property Risk Analysis (the 'Forward Look')

- Is there a potential conflict of interest for the valuer in providing a valuation figure for regulatory purposes and advice on future market changes?
- Are valuations appropriately instructed?
- Are valuations provided in a manner that gives clients sufficient forward-looking

quantitative analysis on risks and their impact on investment worth, in addition to the objective opinion of current value?

- Can more be done to ensure clients understand how to instruct additional supporting bespoke risk analysis?
- Do valuers have the tools to deliver this sort of analysis?

Independence and Objectivity

- Are current RICS requirements in respect of valuer independence sufficient? This will focus on valuations for financial reporting (including investment portfolio performance measurement).
- Are there any other material threats to objectivity in valuation that RICS should consider?
- Should valuation firms be required to provide details of their valuation governance structure in their terms of engagement?

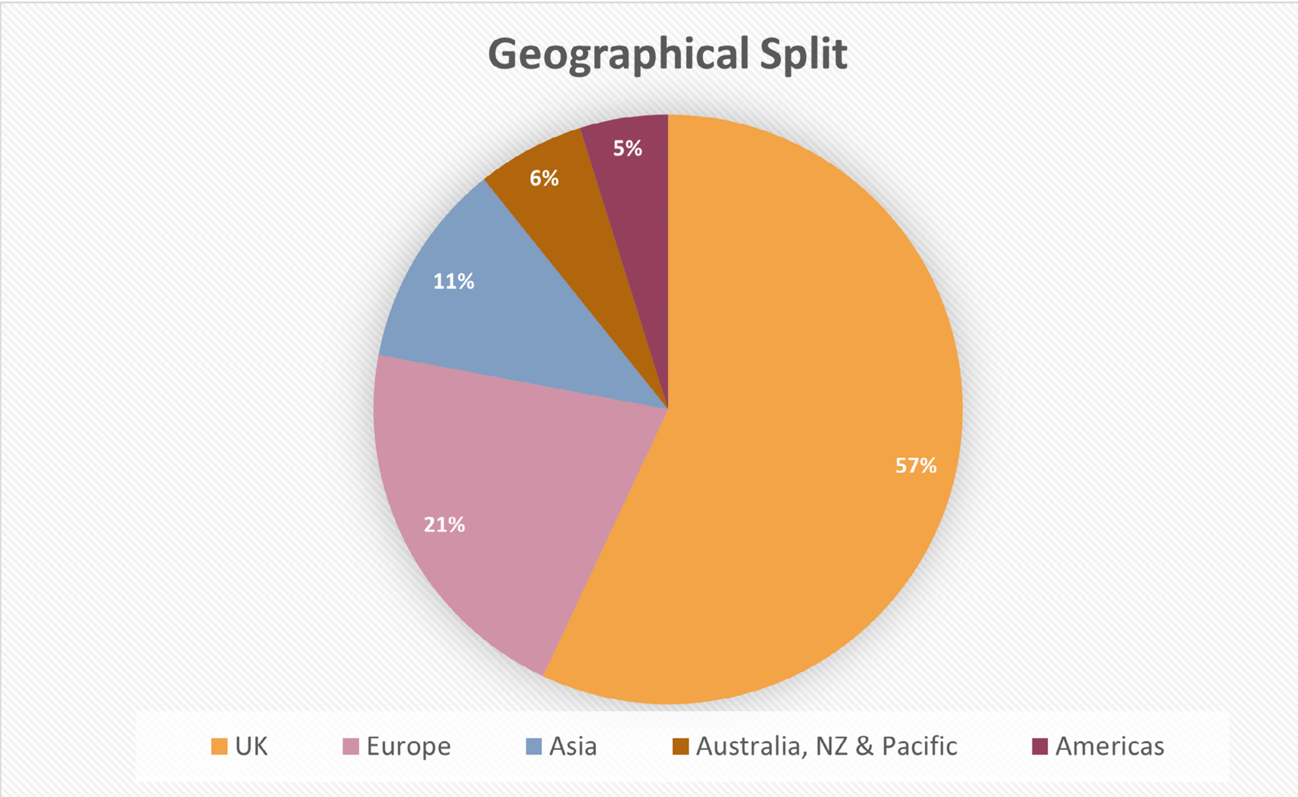
Measuring Confidence

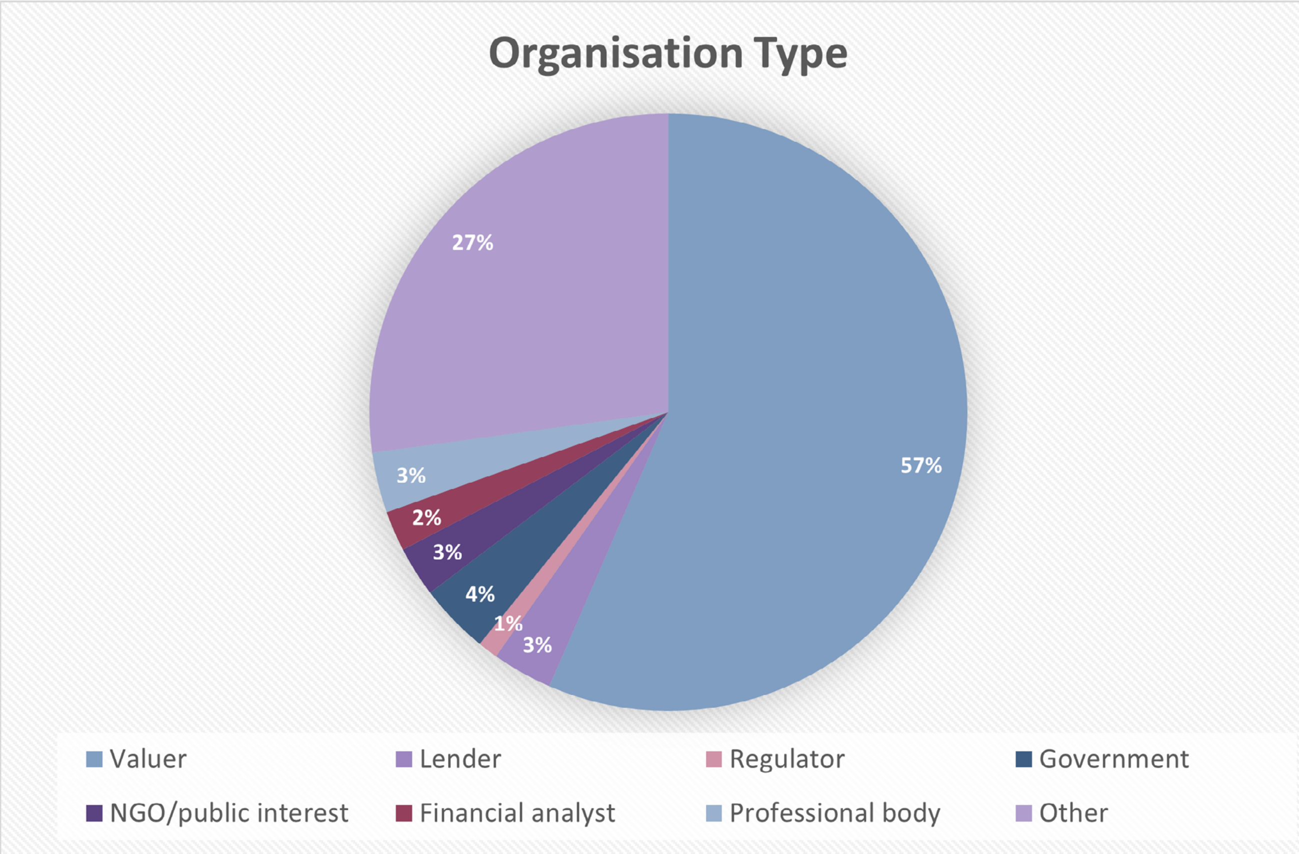
- How can RICS measure market confidence in RICS valuer performance on an ongoing basis?
- Should insights such as the Valuation and sale price report be undertaken more frequently?

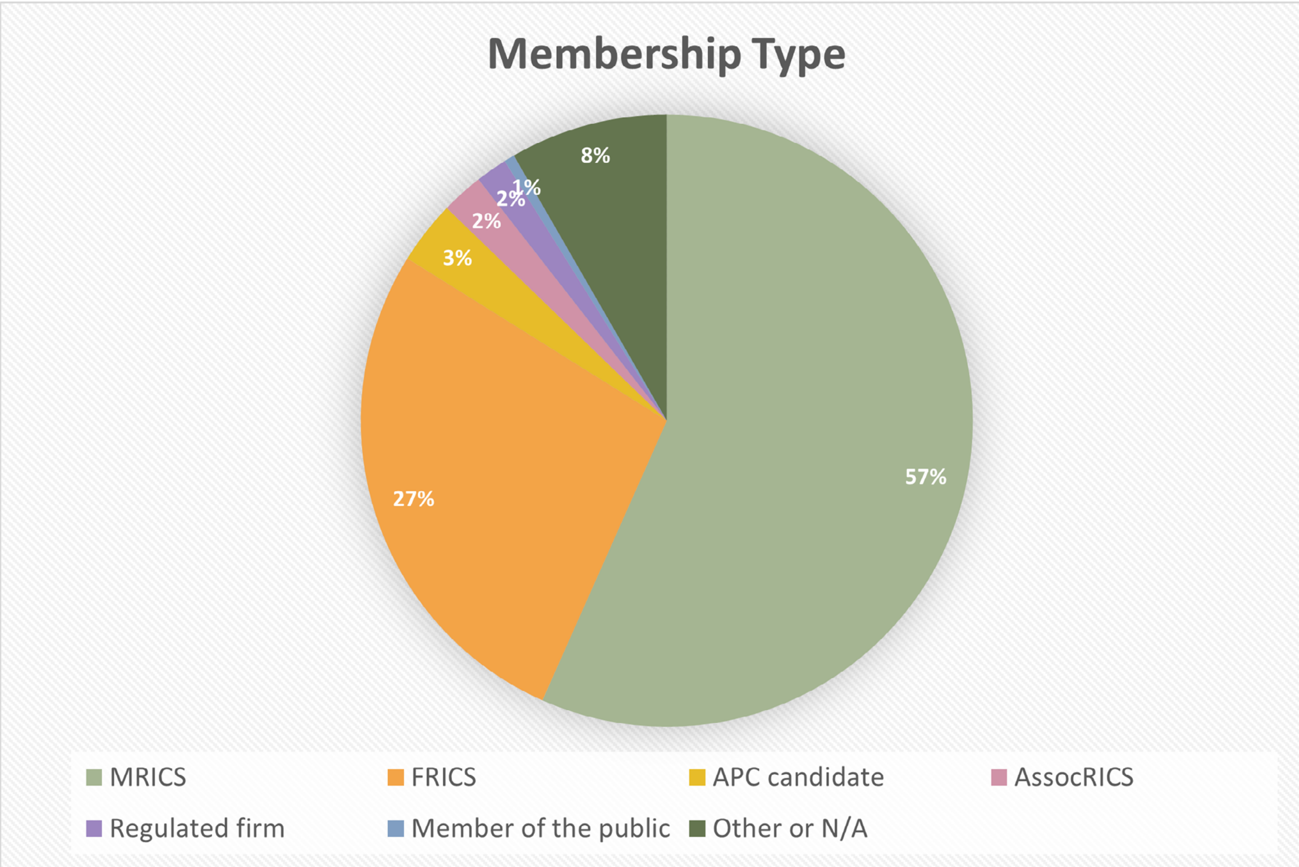
Appendix B – Demographic Breakdown of Responses to the Call for Evidence

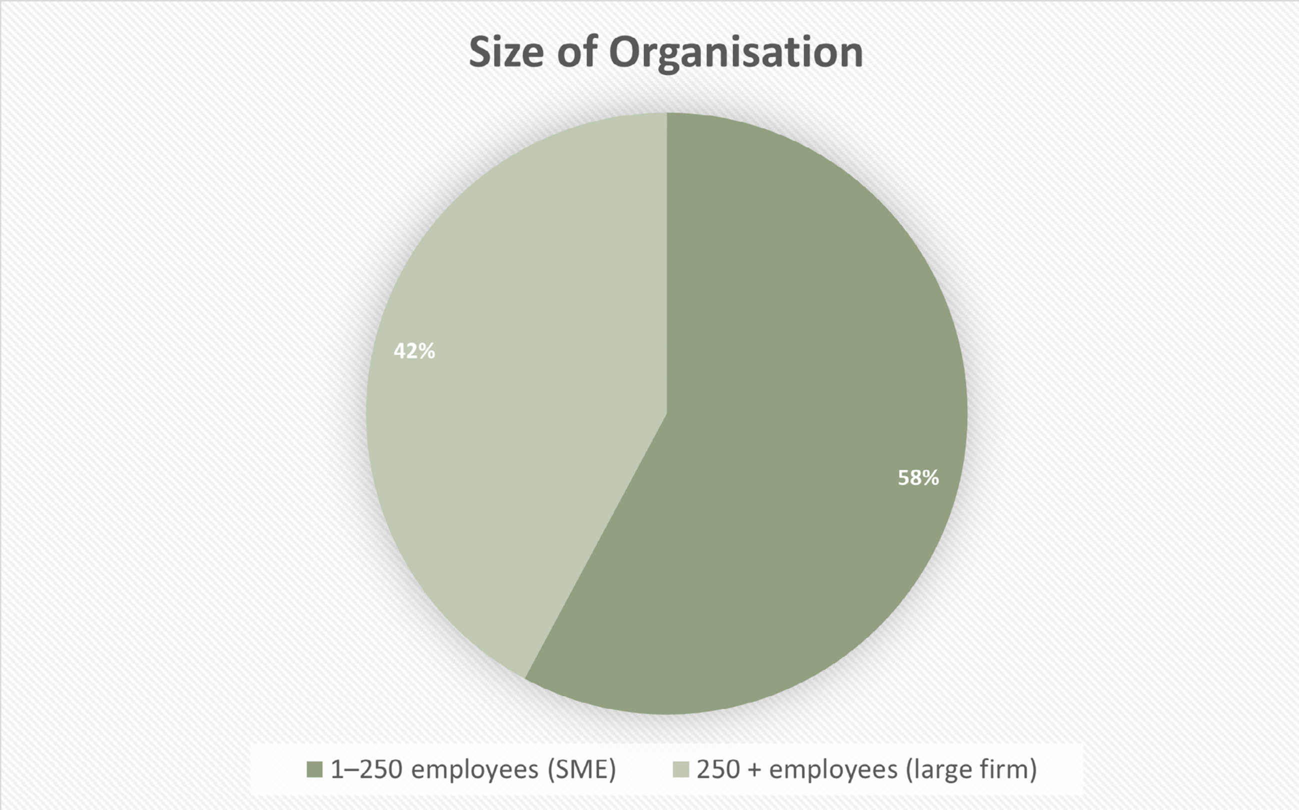
We received a total of 182 responses to the consultation questionnaire. These were predominantly received via the RICS iConsult platform (161 responses), with the rest being received via email. The consultation was open from 12th December 2020 until 31st March 2021.

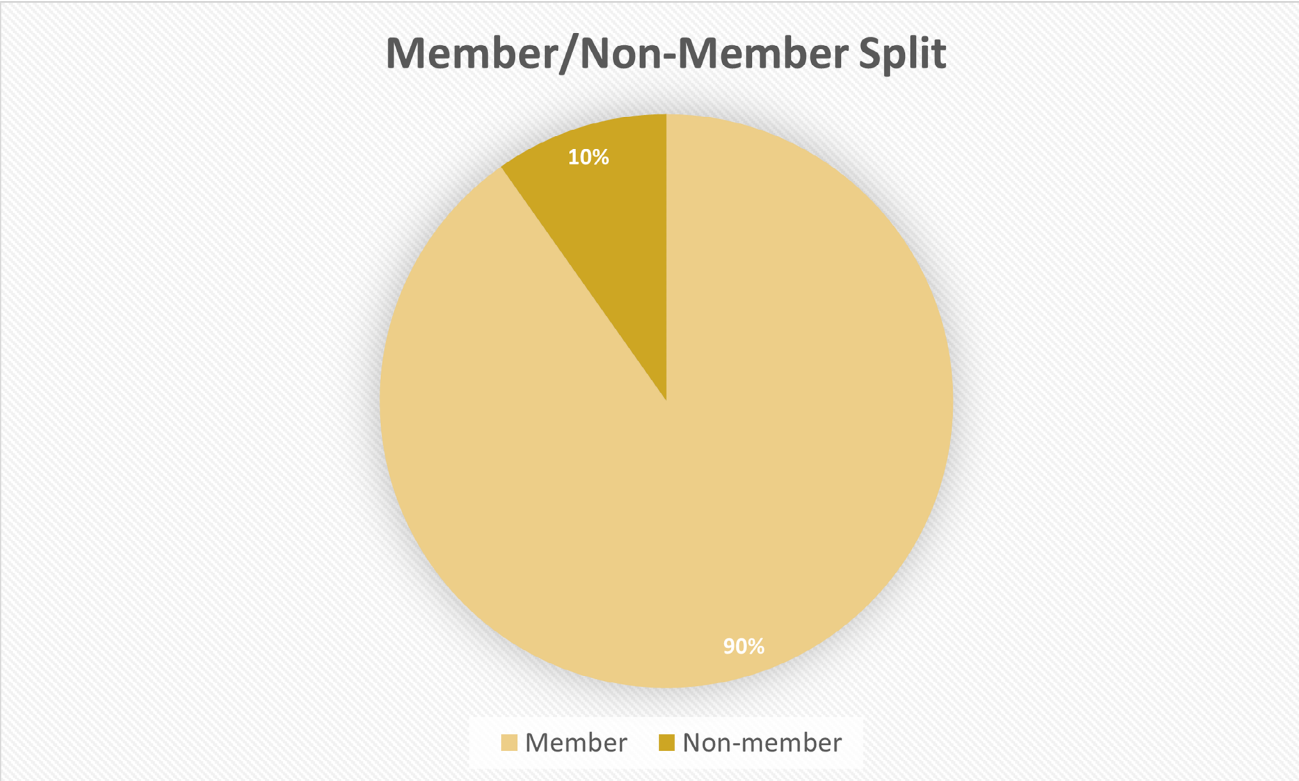
RICS runs many consultations a year on each publication of a guidance note, professional statement or code of practice, as well as for other projects. The response rate of 182 is high, and as shown below, these were received from across the world and from those in varying sectors, all relating to investment valuations.

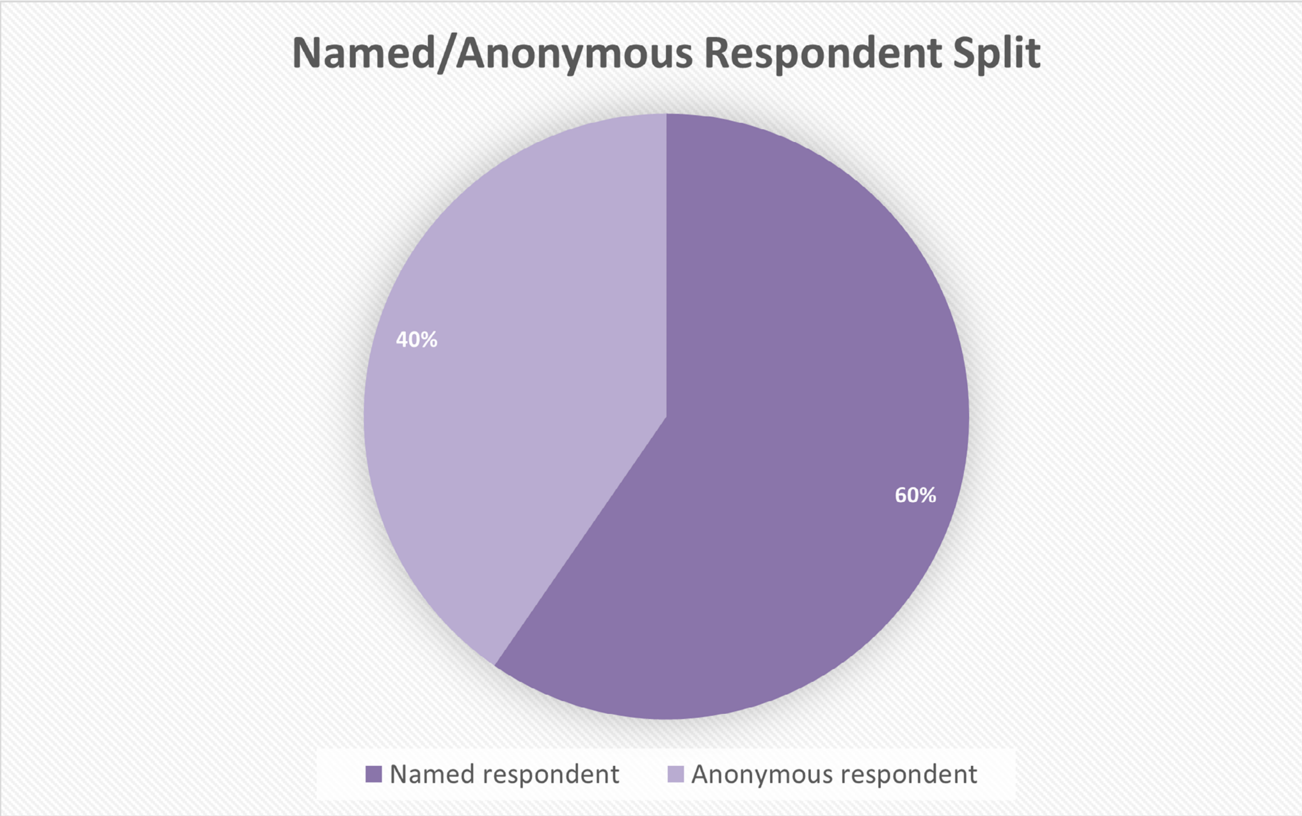


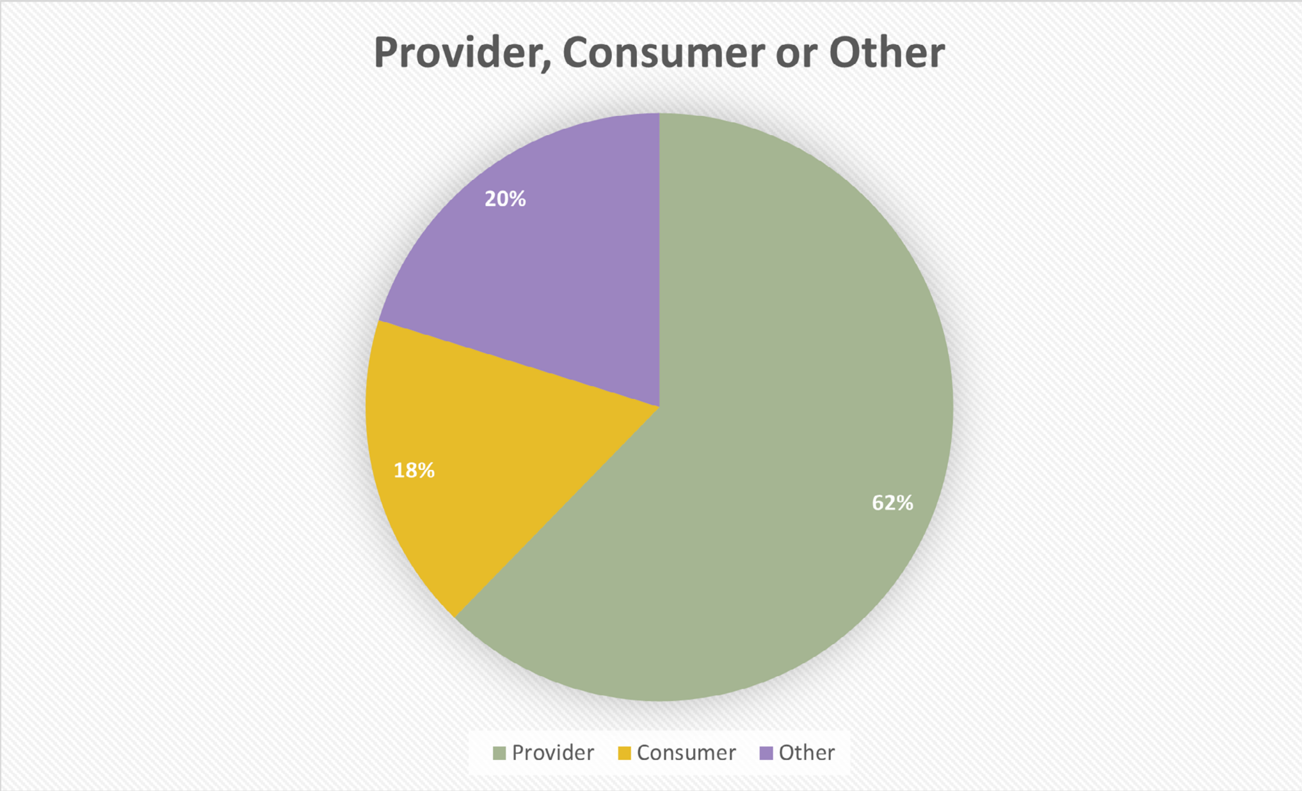

Organisation Type
27%
57%
3%
2%
3%
4%
1%
3%
Valuer
Lender
Regulator
Government
NGO/public interest
Financial analyst
Professional body
Other


Membership Type
8%
1%
2%
2%
3%
27%
57%
MRICS
FRICS
APC candidate
AssocRICS
Regulated firm
Member of the public
Other or N/A


Size of Organisation
42%
58%
1–250 employees (SME)
250 + employees (large firm)


Member/Non-Member Split
10%
90%
Member
Non-member


Named/Anonymous Respondent Split
40%
60%
Named respondent
Anonymous respondent


Provider, Consumer or Other
20%
18%
62%
Provider
Consumer
Other

Appendix C – List of Respondents to the Call for Evidence

We received almost 200 responses to the Call for Evidence. Many responses received were anonymous, and not all gave express permission to publish their name or firm name. Those that did are listed below.

Peter Pereira Gray and RICS and are extremely grateful to all who took the time to respond.

- Aberdeen Standard Investments Ltd.
- Adamos Karantonis & Associates LLC
- Andrew Scott Robertson
- Arca PRM
- Atherstone St. James Ltd.
- AURA REE Portugal
- Avison Young
- Aviva Investors
- Bank of Ireland
- Birmingham City University
- British Property Federation (BPF)
- Broll Nigeria
- Capital Chartered Surveyors
- CBRE
- CDLH Surveyors Limited
- ChatelainXpert
- Chess Associates
- Chesterton Corporate Property Advisers
- CHFT Advisory & Appraisal
- CKE Property Ltd.
- Colliers International
- CREFC
- CREFC Europe
- Cushman & Wakefield
- Daniells Harrison
- Deloitte
- Derwent London
- Deutsche Bank
- Gerald Eve
- Ghebbi Associates
- Global Appraisal Tech (GAT)
- Grant Thornton UK LLP
- Hammerson
- Helios Real Estate
- Holt Commercial
- INREV
- Israel Government Valuation Office
- J Raymond Welch Surveyors
- Jex Surveyors
- JLL
- KappaSigma Partners
- Knight Frank
- Knight Freeman
- KPMG
- LaSalle Investment Management
- Lloyds Banking Group
- Loan Market Association (LMA)
- Mason Owen

- Metro Builders
- Ministry of Finance - Valuations Department
- MJ International
- Montagu Evans
- National Certified Valuators Company
- National Land Agency
- Nihon Tochi-tatemono Co. Ltd.
- NMBS
- Pandox
- Philip Walker Consulting Limited
- Profidis
- Public Investment Fund
- Price Waterhouse Coopers Middle East
- Savills
- Segro
- Society of Chartered Surveyors Ireland
- Solum Property Solutions
- Spalding and Co
- SRK Consulting
- TAQEEM
- University of Reading
- University of Sri Jayewardenepura, Sri Lanka
- Vail Williams
- Valuology
- VARE Consulting
- Vayati Systems and Research Inc
- Valuation Office Agency
- Vocational Training Council, Hong Kong
- VSI Appraisal Group

Appendix D – List of Roundtable Participants

A number of virtual roundtables were held on the four themes of the Valuation Review: four focusing specifically on each theme, and four for the major global regions in which all themes were discussed.

Peter Pereira Gray and RICS would like to thank everyone who participated in these roundtables.

63 individuals attended the eight roundtables, which are detailed below.

Valuation Methodology Roundtable

Date: 19th January 2021. Number of attendees: 11. EAG attendees: 11.

Measuring Confidence Roundtable

Date: 11th February 2021. Number of attendees: 11. EAG attendees: 8.

Property Risk Analysis Roundtable

Date: 16th February 2021. Number of attendees: 7. EAG attendees: 8.

Independence and Objectivity Roundtable

Date: Friday 19th March 2021. Number of attendees: 11. EAG attendees: 9.

Americas Roundtable

Date: Thursday 11th March 2021. Number of attendees: 13. EAG attendees: 7.

Middle East and Africa Roundtable

Date: Thursday 25th March 2021. Number of attendees: 4. EAG attendees: 5.

Europe Roundtable

Date: Thursday 29th March 2021. Number of attendees: 7. EAG attendees: 8.

Asia Roundtable

Date: Thursday 14th April 2021. Number of attendees: 9. EAG attendees: 5.

Appendix E – List of Expert Advisory Group (EAG) Members

The Expert Advisory Group members were independently appointed by the Chair of the Review, Peter Pereira Gray. RICS is grateful for the time and energy the EAG have dedicated to this review.

- Michael Brodtman FRICS, *Chairman UK*, CBRE Ltd.
- David Franklin, *Managing Director, Belonging & Support*, The Institute of Chartered Accountants in England and Wales (ICAEW)
- Sarah Fromson, various independent non-executive roles, including *Director of Arrowstreet Capital* and *Director of Quilter Investors Ltd.*
- Paul Kennedy, *Managing Director – Global Alternatives*, J. P. Morgan Asset Management
- Marc Mogull, *Chairman and Chief Investment Officer*, PineBridge Benson Elliot LLP
- Tim Mould QC, *Planning, Environmental and Public Law Specialist*, Landmark Chambers
- Isobel O'Regan, *Director – Commercial*, Savills Ireland
- Mike Prew, *Managing Director*, Jefferies LLC
- Sandra Robertson, *Chief Executive and Chief Investment Officer*, Oxford University Endowment Management Ltd.
- Rebecca Worthington, *Chief Financial Officer*, Canary Wharf Group Plc

Appendix F – A Brief Overview of the Valuation Process

Below is a brief overview of the valuation process. It is purposefully brief as it is solely to provide background to the Review. This is a simplification and there are many skills and nuances that valuers need to be aware of.

RICS sets out the detail of what is expected from valuers in the Red Book. However, in short there are four key stages to a valuation:

1. **Terms of engagement** – Following the client's initial request for a valuation, the valuer and client agree various terms for undertaking the exercise, which are confirmed in writing by the valuer. These terms of reference include, among other aspects, the identification of those involved, the valuation date, the nature and extent of the valuation, the format of the report, and the basis of the fee.

2. **Inspection and investigation** – The valuer undertakes various inquiries in respect of the subject property. There are generally four main ways the valuers may undertake this: an inspection of the property (ranging from a full on-site inspection to an external 'drive-by' inspection), a property analysis to verify information from the client and other sources, market research (consideration of the relevant market), and a search of available public information. An important part of valuation investigation is data handling and interpretation. The data that is obtained from the inspection and investigation is crucial, and to a certain extent the accuracy of the final valuation outcome is determined by the correct and most relevant dataset being available from the client and during the enquiries process. However, obtaining the right data is often challenging for valuers. There is a need to identify and qualify which data is relevant, translate the raw data into usable outcomes, and interpret the outcomes into explainable information for the client.

3. **Determining the valuation basis, approach, method, and model** – These are the building blocks for the numerical element of valuation. The basis should be agreed in the terms of engagement, as this determines the valuation perspective (such as worth to a particular individual, or alternatively a market value). There are three principal approaches to valuation: market, income, and cost. The selection of approach is made by the valuer to reflect the valuation purpose, basis, and other circumstances. The method of valuation reflects the general principles used to calculate value and the model is a template for the detailed calculations.

4. **Reporting** – In terms of a single valuation figure, the final output of the valuation process is the valuation report. However, the valuation report is more than a figure and should be read in conjunction with the overall context of the report and the supporting evidence provided, including any limitations, assumptions, and special assumptions.

Appendix G – Literature Review

As part of the insight-gathering exercise, and to help inform the findings and recommendations set out in this Review, I consulted several reports, articles, websites, and standards including:

- Brydon Review (2019)
- The Carsberg Report, Property Valuation, RICS (2002)
- Carsberg Review of Residential Property – Standards, Regulation Redress and Competition in the 21st Century, RICS, Association of Residential Letting Agents, National Association of Estate Agents (2008)
- Competition and Markets Authority Review of Audit (2018)
- CP20/15: Liquidity mismatch in authorised open-ended property funds, Financial Conduct Authority (2020)
- Hart v Large – too much information? [2021] EWCA Civ 24, Clyde and Co (2021)
- Has COVID-19 changed how retail space is valued forever? RICS MODUS, February 2021
- Independence v objectivity: what is the difference? ICAEW, 2021
- Independent Review of the Financial Reporting Council (2018 – Sir John Kingman)
- IVSC Perspectives Paper: Challenges to Market Value (2021)
- The Mallinson Report, Commercial Property Valuations, RICS (1994)
- Mandatory Performance Framework for the Certified in Entity and Intangible Valuations Credential (2017)
- Pricing to market – Property valuation revisited: the hierarchy of valuation approaches, methods and models, French and Gabrielli (2018)
- PropTech 2020: the future of real estate, University of Oxford Research, 2020
- RICS Valuation – Global Standards (the 'Red Book'), published 2019, effective 31 January 2020
- The Takeover Code (2021)
- The European Group of Valuers' Associations (TEGOVA) – European Valuation Standards (EVS) – Blue Book (effective 2021)
- Top 10 for the 10s Claims against surveyors and valuers, RPC (2020)
- Uncertainty in retail property values in the UK, Craig Davies, BDO, January 2020
- Valuation and sale price, RICS [supported by MSCI] (2019)

Summaries of the findings in these articles and reports can be found below.

Brydon Review (2019)

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/852960/brydon-review-final-report.pdf

The Brydon review was published in 2019 and focused on audit quality. There are a number of areas of relevance to this independent Review, specifically:

- Communication and transparency in the audit process and audit report
- Redefinition of audit and its purpose
- Introduction of suspicion as a concept for audit alongside professional scepticism
- Increased use of technology

The Carsberg Report, Property Valuation, RICS (2002)

The Carsberg Report, Property Valuation, focused principally on issues of valuer independence and objectivity but did include some detail around property risk. The report made 18 recommendations in total, with those related to independence and objectivity making up a substantial part. These included:

- References to objectivity and lessons that could be learnt from, for example, Chartered Accountants.
- Suggestion of prohibition of one year for producing a valuation where an introductory fee has been paid to the firm, unless another firm has produced a 'full, formal' valuation between the date the transaction was agreed and the date of the subject valuation.
- Recommendation for declaration of total fee earning relationship with instructing client and length of time they have been carrying out valuations for the client.
- Suggestion that the requirement for valuer's fee earning relationship with any party directly interested in the outcome of a valuation be declared to any party to whom they have a fiduciary duty.
- Recommendation that RICS should publish guidance on good practice in rotating personnel producing valuations.
- Proposal that the Red Book should contain specific guidance on the recording of occasions when a valuer discusses the outcome of the valuation with the client or any other interested party.
- Recommendation for the Red Book to include standards around the conduct and recording of draft valuation meetings.
- Suggestion that there is a guide to the valuation process and Red Book from the client's viewpoint.

The report also suggested RICS establishes an *“acceptable method”* for reporting valuation uncertainty.

In addition, the report included various recommendations related to the interface of valuers, RICS and IPD (now MSCI), including around collation and analysis of valuation data and an annual report on the correlation between valuations achieved and prices observed. One recommendation referenced the need for further information and potential publication of the composition and performance of valuers contributing to IPD. Other recommendations included:

- Endorsement for RICS to create a *“Valuation Monitoring Committee”* and attached regulation.
- Recommendation to publish information paper on valuations with limited information.
- Suggested exemption from Red Book for estate agency valuations should be limited to *“proper circumstances”*.

Carsberg Review of Residential Property – Standards, Regulation Redress and Competition in the 21st Century, RICS, Association of Residential Letting Agents, National Association of Estate Agents (2008)

The Carsberg Review of Residential Property focused principally on property agency and management, making 30 recommendations to a range of market participants, professional bodies, and regulators (not just RICS or its members).

Several recommendations were around providing a more consumer-focused service. A set of principles were referred to:

> *“…that decision makers, legislators and regulators follow three basic principles when formulating proposals for the residential property field:*
>
> - *Simple, transparent information for clients and customers is a primary objective;*
> - *Proportionate control over the service provider rather than the service should encourage and allow innovation; and*
> - *Consistent enforcement and redress should underpin all schemes.”*

There were recommendations related to data providers such as a provision for more information from the Land Registry. It was recommended that:

> *“legislation should be introduced to require the holders of search information to provide that information rapidly and efficiently to all members who wish to have it, at a reasonable price, with the objective of electronic availability online as soon as practicable. The legislation should ensure that information holders compete fairly with private search companies.”*

It suggested that *"consistent enforcement and redress should underpin all schemes."*

A further recommendation was made, suggesting it would be helpful to:

> *"introduce new measures through legislation or regulation to require the production of surveys, home condition reports or valuation reports at particular times. The best approach is to encourage the effective working of the market through helping the people involved in transactions to understand the various possibilities."*

Competition and Markets Authority Review of Audit (2018)

https://www.gov.uk/cma-cases/statutory-audit-market-study#final-report

In 2018, the Competition and Markets Authority (CMA) produced an updated paper on its review of the audit sector. The CMA report makes a smaller number of proposals than the Kingman Review, but the proposals it does make are likely to have a more significant impact on the statutory audit market and are of relevance to this Review of real estate investment valuation.

The main recommendations were that:

- There should be mandatory joint audits, at least in regard to the FTSE 350 (perhaps with some limited exceptions), with one of the pair of auditors to be a 'challenger firm' not from the 'Big Four'.
- There should be a structural or (the CMA's preference) an operational split of firms' audit and non-audit functions. It is to consult on this as well as on whether any split should be applied to challenger firms as well as the 'Big Four'.
- There should be peer reviews of overall financials coupled with shadow audits of risky areas with a view to keeping the statutory auditors 'on their toes'. Like Kingman, the CMA suggested that the newly proposed Audit, Reporting and Governance Authority (ARGA) should target companies considered high risk or deserving more scrutiny.

The Review did not consider it necessary to break up the 'Big Four' and it did not consider changes to mandatory rotation.

CP20/15: Liquidity mismatch in authorised open-ended property funds, Financial Conduct Authority (2020)

https://www.fca.org.uk/publications/consultation-papers/cp20-15-liquidity-mismatch-authorised-open-ended-property-funds

The UK financial regulator, the Financial Conduct Authority (FCA), has sought to address issues around property fund suspension and what is described as the *"illiquidity mismatch"*, where property can be indirectly traded through funds in a very liquid way but the realisation of the funds can be illiquid given the unique features of real estate.

Property is illiquid and value is *"not always readily available"* in some market conditions where *"fund units cannot be priced with confidence on a daily basis"*.

Valuation uncertainty can lead to fund suspension. Funds have suspended on several occasions in recent years.

An earlier consultation (CP18:27) considered new rules, PS19/24, which became effective on 30 September 2020, requiring an authorised property fund to be suspended when there is material uncertainty over the valuation of more than 20% of its assets.

Some funds are required to suspend dealing where the Standing Independent Valuer (SIV) expresses material uncertainty regarding 20% of the scheme's property.

A suggested solution to fund suspensions in the subject consultation was the introduction of notice periods for fund withdrawals in order to avoid further suspensions and, where possible, increase/protect returns.

Hart v Large – too much information? [2021] EWCA Civ 24, Clyde and Co (2021)

https://www.clydeco.com/en/insights/2021/02/hart-v-large-too-much-information-2021-ewca-civ-24

A specific recent case against a valuer has highlighted the difference between the provision of information and advice covered in this article.

It covers the distinction between 'advice' and 'information', and the context of the SAAMCo case precedent. This includes commentary on where a surveyor should make the distinction in their terms of engagement.

It concludes that the case is "a warning to surveyors who fail to advise prospective buyers on the need for further investigations when any warning signs may be present".

Has COVID-19 changed how retail space is valued forever? RICS MODUS, February 2021

https://ww3.rics.org/uk/en/modus/built-environment/commercial-real-estate/has-covid-19-changed-how-retail-space-is-valued-forever-.html

A recent RICS Modus article looked at the difficulties in the retail market and how these reflected wider valuation challenges. The following points were made:

> *"In the less-favoured parts of the sector there is little transactional evidence upon which appraisers can base their valuations."*
>
> *"Valuing without comparable sales data requires more legwork and imagination, observes Bruce Kellogg FRICS, Atlanta-based managing director at MG Valuation. 'You have to interview people in the market like brokers and then base your appraisal on that information even if you have no sales. Appraisers are being challenged right now to do their homework and come up with conclusions that they never had to before.'"*

"As a result of the pandemic landlords are increasingly accepting a share of the downside risk with retailers, either through COVID clauses in leases, that reduce rents in the event of government-mandated shutdowns, or through charging turnover-based rents. That poses a challenge for valuers, says Sara Duncan, UK head of valuation and advisory services at Colliers International. 'The difficulty with valuing on turnover rents is that there is not much information out there. But it is possible. We need a standard approach so that there is a market tone, and we have to see some deals so we can understand what multipliers are being paid.'"

Independence v objectivity: what is the difference? ICAEW, 2021

https://www.icaew.com/international-accounting-and-auditing/independence-v-objectivity-what-is-the-difference

This article by the ICAEW defines both objectivity and independence in the context of professional auditing services:

"In the current IESBA Code of Ethics 120.1 Objectivity 'imposes an obligation on all Professional accountants not to compromise their Professional or business judgement because of bias, conflict of interest or the undue influence of others'. The current IESBA Code of Ethics definition of Independence explains it as being made up of two elements: 'Independence of mind' and 'independence of appearance'. The former is still defined to include integrity, objectivity and scepticism. The latter is defined as being free from 'facts and circumstances' that would lead a reasonable and informed third party to conclude that integrity, objectivity or scepticism was compromised."

The article also gives an example checklist approach to auditor independence (not intended to be an exhaustive):

"Do staff have any direct/indirect financial interests in the audited entity?

Do any partners or staff have personal, family or business relationships with officers or employees of the audited entity?

Is there actual/threatened litigation between the firm and the audited entity?

Have any staff received non-trivial gifts or hospitality from the audited entity or its staff?

Are there any urgent reporting deadlines that may lead to resourcing issues and pressure from the management of the audited entity?

Does the audited entity have informed management?

Has the audit fee exceeded 15% of the firm's income for two consecutive years?

Are there significant overdue fees from the audited entity?

Is the firm adequately resourced to perform the audit?"

The article confirms that ICAEW advocates "a framework approach to independence" that:

> *"sets out fundamental ethical principles; provides a reasoned analysis of the possible threats to these principles; and gives guidance on the safeguards which may be necessary to mitigate these threats."*

Independent Review of the Financial Reporting Council (2018 – Sir John Kingman)

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/767387/frc-independent-review-final-report.pdf

In late 2018, Sir John Kingman published his review into the Financial Reporting Council.

The Kingman review focused on the regulation of audit. It is useful to understand where failings have happened in the provision of audit services, and reflect on the role of firms versus individuals in providing professional services.

IVSC Perspectives Paper: Challenges to Market Value (2021)

https://www.ivsc.org/perspectives-paper-challenges-to-market-value/

There have been queries in the market and amongst some stakeholders as to the appropriate application and use of valuation on the basis of market value, a topic this paper covers. It concludes that market value is not *"backward looking"* but instead requires the valuer to *"look at all the facts and circumstances; backwards, sideways and into the future."*

- There is reference to using a wider evidence base to establish market value, such as offer price in certain circumstances.
- There are positive conclusions around the application of a valuer's skillset and use of standards.

This paper refers to some of the challenges around uncertainty and risk in relation to valuation inputs:

> *"…because of the difficulty of finding objective evidence to support either the adjustments or the assumptions made. The valuation method used may adjust for input uncertainty. For example, in a discounted cash flow model the cash flow inputs are based on current expectations of future performance and are therefore uncertain. However, market participants' views of the potential risk or reward implied by the expected cash flows differing from those that actually occur in the future can often be reflected in the discount rate applied."*

The Mallinson Report, Commercial Property Valuations, RICS (1994)

The Mallinson Report covered methodology in detail and made the following recommendations.

RICS should develop a common professional standard for the all-risk yield methodology and work on *"codifying and disciplining"* discounted cash flow (DCF) techniques, as well as on *"parameters"* for the profits method of valuation.

RICS should work with IPD (now MSCI) to research techniques that allow for the expression of *"worth"* (also now known as investment value).

Valuation uncertainty is referenced a number of times in the current Review evidence and is referenced here in an earlier report commissioned by RICS into commercial property valuations.

It suggested the development of a *"universal approach"* to valuation techniques for *"expressing degrees of uncertainty"*, to be led by RICS. It recommended advisory guidance from RICS on circumstances where a valuer should warn of *"abnormal uncertainty"*.

It recommended using the principle that the valuation process should be *"transparent and explicable in terms comprehensible to clients and other users"*.

It included the statement that:

> *"the valuer is seen as an 'expert' outside the auditing process. We think that is wrong … valuer and auditor must be as one and mutually supportive. Whilst the auditor has the ultimate statutory responsibility, and that should not be changed, the valuer must contribute to ensuring a 'true and fair view' is shown."*

Mandatory Performance Framework for the Certified in Entity and Intangible Valuations Credential (2017)

https://ceivsite.files.wordpress.com/2017/01/final-mandatoryperformanceframework-1-17.pdf

The Mandatory Performance Framework for the Certified in Entity and Intangible Valuations credential was developed to address the perception of issues with the training and expertise of some professionals undertaking intangible asset valuations.

> *"Regulatory, creditor, and shareholder concerns as well as public perceptions are driving the need for valuation professionals to conduct themselves with professionalism and demonstrate professional competence."*

Technical standards and guidance are seen to address the 'how-to' question, with training, accreditation, technical guidance, and frameworks for ethical conduct said to address the 'who is to do' question. One area, however, where *"gaps in guidance are believed to still exist relates to performance (that is, addressing the 'how much to do' question)."* The mandatory performance framework provides these parameters.

The framework includes reference to professional competence, valuation engagement, and reporting.

Pricing to market – Property valuation revisited: the hierarchy of valuation approaches, methods and models, French and Gabrielli (2018)

This academic journal paper outlines a three-tier hierarchy for valuation; the basic approaches (income, market cost) defined in IVS; methods, which are *"an overall structure for the valuation"*; and models: *"the detailed application of a mathematical technique"*.

An example is given of the three-tier hierarchy:

- Approach: Income approach – The income approach provides an indication of value by converting future cash flows to a single current capital value.
- Method: Investment method – Value is based upon an actual or estimated income that either is or could be generated by an owner of the interest. In the case of an investment property, that income could be in the form of rent; in an owner-occupied building, it could be an assumed rent (or rent saved).
- Model: Implicit capitalisation – Where an all-risks or overall capitalisation rate is applied to a representative single period income to determine the capital value,
- Alternative model: Explicit DCF – Where a discount rate is applied to a series of cash flows for future periods to discount them to a present value or capital value.

The piece also covers the frequently raised issue of misunderstanding different valuation bases:

> *"Many users of valuation cannot distinguish between the price that they would get for the property … in the open market … and what they believe the asset is worth to them."*

PropTech 2020: the future of real estate, University of Oxford Research, 2020

https://www.sbs.ox.ac.uk/sites/default/files/2020-02/proptech2020.pdf

Technology features heavily elsewhere in the Review evidence – particularly with reference to data and data access. This research highlights some of the key issues and looks at the extent to which real estate investment is analogous with other types of investment in light of technological improvements.

> *"The growth of indirect private fund vehicles with different styles, debt and asset-backed securitisation, the arrival of REITs, the growth of a derivatives market – all of these developments fed on and demanded a much more quantitative and research-focussed approach to performance measurement and investment strategy; and the rapid globalisation of the real estate industry in terms of investors, sources of capital and advisory services substantially reduced the insularity of the industry and brought increased demands for a*

more research-led product. Growing data availability enabled more finance-grounded quantitative modelling, and valuation software and property and portfolio management systems became computer and technology based …"

However, much of the real estate data needed is held privately and contained within analogue documentation and is not so easy to aggregate or access. Many data providers and exchanges are aiming to become the sole provider of real estate information to facilitate greater market transparency, while making financial gains through charging third party organisations for use of their API. There will be many losers …"

However, open data sets require no permission for such use, in which case information can be scraped and updated in real time, enabling a machine learning-based AVM to refine the accuracy of future predictions. Crucially, these models might avoid the stale valuation problem, as a relationship with stock and bond markets (for example) might be established so that a fall in the financial markets might indicate a fall in house prices even in the absence of comparable transaction evidence. If this produces more realistic asking prices, this would clearly improve liquidity."

RICS Valuation – Global Standards, the 'Red Book', published 2019, effective 31 January 2020

https://www.rics.org/uk/upholding-Professional-standards/sector-standards/valuation/red-book/red-book-global/

The following guidance on rotation policy is included in Red Book Global Standards PS 2:

"Familiarity with either the client or the asset valued could lead to the perception that the member's independence and objectivity have been compromised. This may be addressed by arranging for the rotation of the member who accepts responsibility for the valuation."

PS 2 of Red Book Global Standards includes the following regarding disclosure:

"Where the valuation is of an asset that has previously been valued by the valuer, or the valuer's firm for any purpose, the following disclosures must be made in the terms of engagement, in the report, and in any published reference to the valuation, as the case may be, as set out later below:

- *the relationship with the client and previous involvement*
- *rotation policy*
- *time as signatory*
- *proportion of fees."*

The following specific requirements on rotation policy are also included in PS 2:

"The obligation to disclose the firm's rotation policy will arise only where the member has provided a series of valuations over a period of time … Where it is a first or one-off instruction, it is not necessary to comment on any general rotation policy …

Where the member responsible for the valuation in accordance with this standard holds that responsibility for many years, familiarity with either the client or the asset valued could lead to the perception that the member's independence and objectivity has been compromised. This may be addressed by arranging for the rotation of the member who accepts responsibility for the valuation ….

The method by which a firm arranges for any rotation of those responsible for valuations is for the firm to decide, after discussion with the client if appropriate. However, RICS recommends that the individual responsible for signing the report, no matter the standing of that member in the firm, has that responsibility for a limited number of years. The exact period will depend on:

- *the frequency of valuation*
- *any control and review procedures in place such as 'valuation panels', which assist both the accuracy and objectivity of the valuation process and*
- *good business practice."*

Note the following *"good practice, albeit not mandatory"* recommendation is made:

"…to rotate valuers at intervals not exceeding seven years … If a firm is of insufficient size to rotate the signatory, or to have in place 'valuation panels', other arrangements could be made to comply with the principles of this standard. For example, where the same valuation instruction is undertaken on a regular basis, an arrangement for the valuation to be periodically reviewed at intervals not greater than seven years by another member would assist in demonstrating that the member is taking steps to ensure that objectivity is maintained and thus may retain the confidence of those relying on the valuation."

Red Book Global Standards PS 2 section 4.2 currently defines the mandatory duties of a Compliance Officer as ensuring:

"a) the individual(s) acting for conflicting clients must be different – note that this extends to secretarial and other support staff

b) such individuals or teams must be physically separated, at least to the extent of being in different parts of a building, if not in different buildings altogether

c) any information or data, however held, must not be accessible to 'the other side' at any time and, if in a written form, must be kept secure in separate, locked accommodation to the satisfaction of the compliance officer, or another senior independent person, within the firm *d) The compliance officer or other senior independent person:*

i) should oversee the setting up and maintenance of the arrangement while it is in operation, adopting appropriate measures and checks to ensure it is effective

ii) must have no involvement in either of the instructions and

iii) should be of sufficient status within the organisation to be able to operate without hindrance and

e) there should be appropriate education and training within the firm on the principles and practices relating to the management of conflicts of interest."

The Red Book comments on what has come to be known as the 'forward look' in VPS 4 as follows:

"As markets continue to develop and advance, and as clients' needs continue to grow in terms of sophistication, additional demands are being placed on valuers to provide advice involving some element of prediction or forecast. Great care is needed to ensure that such advice is not misunderstood or misrepresented, and that any sensitivity analysis is carefully presented so as not to undermine the basis of value adopted."

The Takeover Code (2021)

https://www.thetakeoverpanel.org.uk/the-code/download-code

The Takeover Panel develop and apply The City Code on Takeovers and Mergers (also known as the 'Takeover Code'). This comprises appropriate business standards and principles for fairness to shareholders and an orderly framework for takeovers. The rules are backed by a statutory framework in the UK. The Code is based upon six General Principles, also set out in Part 1 of Schedule 1C to the Companies Act 2006.

In addition to the General Principles, the Code contains a series of rules, the most important of which are summarised on the Takeover Panel's website. Examples include:

- *"Profit forecasts, quantified financial benefits statements and asset valuations must be made to specified standards and must be reported on by Professional advisers.*
- *The offeree company must appoint a competent independent adviser whose advice on the financial terms of the offer must be made known to all the shareholders, together with the opinion of the board.*
- *Favourable deals for selected shareholders are banned.*
- *All shareholders must be given the same information.*
- *Misleading, inaccurate or unsubstantiated statements made in documents or to the media must be publicly corrected immediately.*

- *Stringent requirements are laid down for the disclosure of dealings in relevant securities during an offer."*

The European Group of Valuers' Associations (TEGOVA) – European Valuation Standards (EVS) – Blue Book (effective January 2021)

https://tegova.org/european-valuation-standards-evs

RICS is not the only standard setter for valuation, some end users additionally or instead following TEGOVA standards for example.

TEGOVA more directly prescribes the interface between valuation advice and European legislation.

It includes a detailed Europe-wide residential valuation standard, differing from Red Book Global Standards, which does not provide advice sector by sector (note the Red Book national supplements do have sector-specific standards).

TEGOVA includes specific references to energy efficiency and sustainability.

Top 10 for the 10s Claims against surveyors and valuers, RPC (2020)

https://www.rpc.co.uk/perspectives/real-estate-and-built-environment/top-10-for-the-10s-claims-against-surveyors-and-valuers/

The ultimate failing of market confidence in valuer performance can in limited circumstances result in litigation. This article suggests that: *"the 10s were a busy time for claims against surveyors and valuers"*. It also included:

- A summary of 10 important cases related to valuation and surveying between 2010 and 2020.
- A suggestion of how principles and guidance from the cases will *"help anyone facing a claim to navigate the key issues and to prepare the arguments they need to deploy in their defence."*

Uncertainty in retail property values in the UK, Craig Davies, BDO, January 2020

https://www.bdo.global/en-gb/blogs/valuations-blog/january-2020/uncertainty-in-retail-property-values-in-the-uk

Retail markets have been referenced as one where changing behaviours, technology, and market understanding have led to discussion of the correct valuation methodology. This article discusses this, stating:

> *"…there is a strong case for moving away from the UK centric yield basis of real estate valuation for retail assets and to treat the sector as "trading assets" and value using techniques such as Discounted Cash Flow ("DCF"). This is the approach adopted by mainland Europe and has been the standard in the US for more than 30 years…*

…More weight should be attributed to the DCF method of valuation as this can be used to reflect anticipated changes in the market. DCF is a forward-looking approach which seeks more and better support for core assumptions.”

Valuation and sale price, RICS [supported by MSCI] (2019)

https://www.rics.org/globalassets/rics-website/media/knowledge/research/insights/valuation-and-sale-price-march-2019-rics.pdf

References have been made indirectly and directly in some of the current Review evidence to valuation and sale price exercises carried out by RICS in conjunction with MSCI (and previously IPD). The latest of these, from March 2019, showed that the weighted average absolute differences between market adjusted valuation and sale price of commercial property in the UK, between 1999 and 2017, ranged from 7.1% to 11.2%.

Analysis varied dependent on geography and sector.

The scale of the market and observable data varied yearly as a result of wider market impacts.

Appendix H – Glossary

Automated valuation model	The machine application of one or more mathematical techniques to provide an estimate of value of a specified asset at a specified date, often accompanied by a measure of confidence in the accuracy of the result, without human intervention post-initiation.
Discounted cash flow	A valuation model that seeks to determine the viability and investment value of a real estate investment property by examining its future net income or projected cash flow from the investment, and then discounting that cash flow to arrive at an estimated current value of the investment. A discount rate is used to derive the net present value of the expected future cash flows. For the evaluation of real estate investments, the discount rate is commonly the real estate's desired or expected annual rate of return.
Investment property	Land or a building (including part of a building) – or both – that is: held to earn rentals, for capital appreciation, or both; not owner-occupied; not used in production or supply of goods and services, or for administration; and not held for sale in the ordinary course of business. Investment property may include investment property that is being redeveloped.
Investment valuation	An opinion of market value applied to investment properties that share a common characteristic: that the value is based upon an actual or estimated income that either is, or could be, generated by an owner of the interest, generally in the form of rent. Investment valuations can be classified as being derived from either an 'explicit method', whereby the expected cash flows are determined and discounted at a target rate of return, typically adopting a discounted cash flow approach, or an 'implicit method' consisting of using a capitalisation and current market rent based on comparable evidence.
Market value	Market value is a basis of value that is internationally recognised and has a long-established definition. It is the estimated amount for which an asset or liability should exchange on the valuation date, between a willing buyer and a willing seller, in an arm's-length transaction, after proper marketing and where the parties have each acted knowledgeably, prudently, and without compulsion.

Price	The amount either asked or paid, and can be established as a matter of fact from market evidence. Price is an objective term. Similar measures such as worth and value are matters of opinion but may need to be established to aid decision-making.
Property risk testing/analysis	Involves evaluating and considering the impact of risk factors associated with real estate investment to make accurate underwriting and investment decisions, seeking to avoid potential future losses and liabilities. In terms of real estate investment, risk analysis is typically concerned with the following risks: market, economic, cash flow, legal, property management, leasing, tenant, construction, and location factors.
Scenario modelling	A process of examining and evaluating events or scenarios (favourable or unfavourable) that could take place in the future and predicting the various feasible results or outcomes on real estate, usually measured in terms of impact on cash flow (including rent), net present value, and various investment performance indicators. IVS recognises that valuers may apply multiple scenarios of, for example, possible future cash flow.
Sensitivity analysis	The investigation of how any two measures vary with a change in one of the assumptions. It acts as a visual what-if analysis of the unknown variables related to real estate and how they can change throughout the life of the investment. These variables can include, but are not limited to, the price of the property, holding period, capitalisation rate at sale, lease renewal probability, vacancy rates, interest rate, debt yield, and more.
Statistical analysis	The collection and interpretation of data to uncover patterns and trends. Red Book Global Standards VPS 5 states that: *“Valuation methods may include a range of analytical tools or techniques as well as different forms of modelling, many of which involve advanced numerical and statistical practices. In general, the more advanced the method, the greater the degree of vigilance needed to ensure there is no internal inconsistency, for example, in relation to the assumptions adopted.”*