RICS Valuation – Global Standards 2017

A guide to key changes & basis of conclusions

Purpose

This document has been prepared to accompany publication of the *RICS Valuation – Global Standards 2017*, or the RICS Red Book as it is commonly known**, in order to explain the rationale behind the more significant changes made in this new edition, which takes effect from 1 July 2017.** Specifically, it addresses the main refinements made in consequence of the responses received to the public consultation. **It is emphasised that it has been produced purely to assist the reader and does not form part of the standards.**

RICS Valuation Professional Group

1 June 2017

Overview

The **main reason for issuing a new global edition of the RICS Red Book is to take account of the significant changes to the *International Valuation Standards* (IVS) introduced in the IVS 2017 edition, which the Red Book adopts and applies**. The rationale for the IVS 2017 changes has already been set out in a comprehensive document issued by the International Valuation Standards Council and does not need to be repeated here.

The public consultation on the 2017 global edition of the RICS Red Book opened on 21 February and closed on 3 April 2017. Over 120 responses on single or multiple points were received from individuals, firms and other organisations containing some very constructive observations and suggestions. **This document focusses only on the more significant changes** made, but a number of minor textual refinements put forward by commentators have also been adopted, which improve the overall clarity. RICS is very grateful to all those who responded.

It is now more than 40 years since RICS first published *Guidance notes on the valuation of assets*, since when the content and coverage of what is now widely known as the RICS Red Book has progressively developed. Over that period international standards in valuation and allied areas of professional activity have also become more firmly established and continue to evolve, a process to which RICS has itself substantially contributed. The RICS Red Book retains an important role in drawing together these various international standards and requirements relevant to valuation and ensuring their effective implementation by RICS members through the addition of RICS-specific material. The formal title of this new edition, *RICS Valuation – Global Standards 2017*, is designed to recognise this broadening context, within which RICS members continue to operate to the highest professional standards.

Comments on the individual Red Book sections follow below.

Introduction

Consultation responses underline that members continue to look for absolute clarity as to what is mandatory in the Red Book and what is advisory, and that some doubts or difficulties are, or would be, caused by the plethora of descriptions of official RICS material reflected in the Consultation Draft. These criticisms are recognised as having a good deal of validity, and the opportunity has been taken in the final version to:

- be more consistent in the language used (for example, now referring to 'these global standards' throughout)
- **add additional explanation at paragraphs 14 and 16 of the Introduction on the status of the content**
- remove 'document definition' terms from the main Glossary and instead substitute a more straightforward summary in a new second part of the Glossary
- **make clear that the individual PSs and VPSs each constitute a 'mandatory standard'**

- **introduce an explanatory 'text box' at the start of each VPGA reinforcing that they are advisory even though for the convenience of users they include some cross-references to mandatory material.**

The opportunity has also been taken to recognise that, as the definitive version of the RICS Red Book on any given day is to be found on the RICS website, RICS will seek to ensure that members are aware of any changes made over time by highlighting them in the relevant professional group newsletters or through other established electronic communication channels at the point in time the changes are made.

Glossary

Minor changes have been made to minimise overlap between RICS-defined technical terms and IVS-defined terms (the latter being contained in Part 6 of the Red Book). **Cross-references to the relevant IVS have been added where appropriate**. For the avoidance of doubt, **'real estate'** is the term used in the Red Book as a **general description of land and the built environment**, whereas the (IVS-defined) term 'real property interests' is used to describe assets or liabilities involving, or related to, real estate.

Queries were raised as to whether 'value', 'valuer' and 'valuation' should all be expressly defined. 'Valuer' is defined in the IVS Glossary and 'valuation' in the RICS Glossary, whereas 'value' follows its common dictionary meaning, so no changes to the Consultation Draft were felt to be necessary on this score.

A query was also raised as to whether definitions of 'external valuer' and 'internal valuer' were still necessary or indeed relevant given that the underlying issue is really about independence. This is seen as a fair point, but the terms are retained for the moment partly to recognise that they are used (though not defined) in the IVS and partly to ensure that their usage is not confused with other definitions in jurisdictional legislation or regulation which have to be applied in specific contexts.

To avoid the risk of confusion with the IVS 2017 definition of 'synergistic value', the Red Book now refers consistently to 'marriage value' throughout, including in the RICS Glossary.

Finally, a question was raised as to whether 'independence' and 'objectivity' should be defined. Objectivity is explained, rather than defined, in the IVS Framework at paragraph 40.1, and it is not felt that more needs to be added. Independence is more a relative term, different criteria being used in different contexts to specify and secure that a desired state of independence is met – this is dealt with in more detail in PS 2 and other relevant parts of the Red Book text.

PS 1

An additional paragraph 1.5 brings forward from the 2014 edition the reference to (estimated) **replacement cost figures for assets other than personal property not being regarded as within the scope of the Red Book**. It is hoped that this removes any doubts that may have arisen in consequence of its omission from the Consultation Draft.

Consultation responses differed on the merits of including additional explanatory material on the subject of 'exceptions' drawn from the Question and Answer (Q and A) material published on the RICS website last year. While it is impossible to cover every conceivable situation, nevertheless having regard to the consultation responses and also to the nature and volume of queries directed to the RICS Valuation Professional Group for clarification, which have reduced in overall number since the Q and A material referred to above was issued, it is felt on balance better to retain the additional wording included in the Consultation Draft. A suggested refinement has been taken on board however – while no change has been made to the substantive content, the running order in the last limb of paragraph 5.4 has been altered so that the reference to ‘negotiations’ now (more logically) precedes that to ‘litigation’. In addition, where there is an ‘exception’, the text now makes clear that VPS 1-5 inclusive (not just VPS 1–4) become advisory rather than mandatory.

The text of paragraph 6.2 has been amended to make clear that departures may arise in relation to any of VPS 1–5 inclusive. Paragraph 6.3 provides additional clarification on when and how a departure may arise.

PS 2

The running order has been further refined without making changes to the text other than mentioned below. It is recognised that there is **some overlap with the content of the RICS *Conflicts of Interest* professional statement**, **but this is intended to be helpful to members, reinforcing aspects that are of particular relevance to valuation**.

The heading and **text under paragraph 6.2** has been **altered to refer to** ‘**reliance by third parties**’, since when and how a duty of care may arise depends on the particular facts and circumstances concerned – including the jurisdiction.

Under **Section 7 *Terms of engagement (Scope of Work)***, **where VPS 1 is not mandatory**, the **emphasis is on the preparation of appropriate terms of engagement to suit the specific case** and the maintenance of a record of their agreement in a recognised and acceptable business format. This is as much a protection for members as it is for clients or other users – it is not the intention to impose new burdens on members.

PS 3 *(now deleted)*

As noted above, a number of steps have been taken to ensure clarity between mandatory and advisory material in this new edition, including in particular further clarification of the status of the VPGAs. It is clear from the consultation responses that a mandatory requirement to ‘have regard to’ the VPGAs relevant to the work involved in an individual valuation assignment could have undesirable consequences, for example, constraining members’ ability to give expert evidence in legal proceedings. This risk, and criticism, is acknowledged and so – with the benefit of the clarification already mentioned – it has been decided not to incorporate PS 3 (as proposed in the Consultation Draft) in the final version.

Part 4: Introduction to the VPSs

At the start of Part 4 of the Red Book, an introductory paragraph makes clear that the **valuation technical and performance standards** to be followed by members are **set out in VPS 1–5**, though avoiding an arbitrary distinction between the two categories. Thus, while **VPS 1, 4 and 5 focus more on technical standards** and **VPS 2 and 3 focus more on performance and delivery standards**, their content and running order is designed to correspond with that of the International Valuation Standards, which the VPSs adopt and apply.

A number of consultation responses noted the inconsistent use of bold type in the VPSs, raising some doubt as to what was mandatory and what – if anything – was not. This criticism is accepted and bold type is now used simply for emphasis, highlighting the key principles and also any important cross-references. Thus, each VPS now consists of:

- the key principles or 'rules' that are to be followed and
- how those principles or rules are to be interpreted and implemented.

The entirety of the text of each VPS constitutes the 'standard' – the 'implementation' text is an essential part of understanding and applying those principles and rules to individual valuation assignments, but very obviously not every paragraph will be applicable to every assignment. They have to be applied in a common-sense manner.

VPS 1

Under b) ***Identification of the client(s)*, the paragraph referring to the absence of a 'direct' client has been deleted**, as this is an unnecessary complication that distracts from the key points here.

Rather than insert the Red Book 2014 material regarding the **treatment of portfolios and collections** as a separate new heading under VPS 1 – on which proposal there was criticism in the public consultation responses on the grounds both that it was really about the proper identification of the asset(s) being valued and also was mainly a matter of guidance – it has been decided to include the **key requirement under d) *Identification of the asset(s) or liability(ies) being valued* and retain the guidance material in a VPGA, namely VPGA 9. A corresponding change has been made in VPS 3.**

In relation to **j) *Nature and source(s) of information upon which the valuer will rely***, and to **k) *All assumptions and special assumptions be made***, one of the consultation responses drew attention to the need to differentiate more clearly between reliance on information and, where necessary and appropriate, the making of an assumption. The over-simplified sentence 'information that is accepted as reliable should be referred to as an assumption' is potentially misleading, and has been deleted (with a corresponding amendment at **VPS 3 paragraph 2.2(h)). Information can derive from many sources, and some of it may properly be taken as fact, that is, it does not involve an assumption**. But **other information that cannot be verified** by observation or experience, or the verification of which is limited by the terms of the assignment, **may justify an assumption for the purpose of completing the particular valuation task**.

At n) (now **m**)) ***Restrictions on use, distribution and publication of the report***, a query was raised as to whether **paragraph 5**, somewhat longstanding, has outlived its usefulness. It was agreed that it should be **removed**. The **fuller treatment** of this **topic** to be found in the **implementation paragraphs in VPS 3 k) (now j))** has, however, been **retained** for the time being, though its continued usefulness and relevance will be kept under review.

VPS 2

There was more than one criticism of including material about (physical) measurement in a valuation standard. It is agreed that an appropriate cross-reference to the relevant RICS professional statement is all that is needed. Thus, in paragraph 1.4 of VPS 2 the language used mirrors that in paragraph 3.5 of PS 1. In neither case is it the intention to set out in the Red Book mandatory standards or detailed requirements concerning measurement of real estate.

A number of representations received concerned the coverage of '**sustainability**' (as defined in the RICS Glossary) in VPS 2 including the recommendation that sustainability data be captured for the purpose of future comparability. External observers actively support raising the profile of 'sustainability' in relation to real estate, while members recognise its growing significance as a potential or actual market influence, but express concern about imposing additional burdens (and costs) that may not be relevant in individual valuation assignments. **The text has been refined to stress the importance of awareness of 'sustainability' factors wherever relevant, but making explicit that the collection of data not required for fulfilment of the particular assignment** is not mandatory. It must always be a matter for the valuer's judgement in the particular context, informed by the views and/or objectives of the client.

VPS 3

In VPS 3 some minor re-ordering of some of the supporting 'implementation' material has been undertaken to ensure that the paragraphs concerned appear under the most appropriate relevant heading (for example, material concerning exchange rates/currency has been moved from d) to m)). Also, as noted above in connection with VPS 1, the **material on portfolios and collections is now a subheading of item d), with the associated guidance contained in VPGA 9.**

On e) ***Basis(es) of value*, greater discretion is given to the valuer** – where the basis of value is not a market-based figure and the valuation is materially different from market value – **as to whether an explanatory statement should be added**. This **must** necessarily **depend on the facts and circumstances**.

At j) (now i)) ***Restrictions on use, distribution and publication***, the **requirement to include all assumptions and special assumptions in the body of the report is retained**, **but the text has been amended so that only the special assumptions must also be included in any executive summary**. The implementation paragraphs in the Consultation Draft relating to various other matters have been dropped, as the topics concerned are – where necessary – sufficiently covered under the appropriate dedicated headings.

At n) (now m)) ***Amount of the valuation or valuations*, a clarification has been introduced** regarding reporting asset by asset or otherwise. This **underlines that it will depend on the circumstances and on client preferences**. Some other minor edits have also been made to improve the readability of the text.

The subject matter of p) (now o)) **Commentary on any material uncertainty** in relation to the valuation where it is essential to ensure clarity on the part of the valuation user raised a significant amount of comment. Both the existing (Red Book 2014) and proposed (Red Book 2017 Consultation Draft) treatments were felt to have shortcomings, among them the risk that valuers might feel obliged to include a comment on uncertainty in more cases than would be justified, or even to adopt a 'standard clause' at times when markets were less active or less consistent. Views also diverged on whether the issue should be covered only by guidance, or whether at least some mandatory requirement was proper. This has been considered carefully and the **Red Book 2017 will contain a mandatory requirement to provide commentary but strictly only where the uncertainty is material**, for this purpose **'material' meaning where the degree of uncertainty in a valuation falls outside any parameters that might normally be expected and accepted**. This reinforces the fact that most valuations will be subject to a degree of variation (that is, a difference in professional opinion), a principle well recognised by the courts in a variety of jurisdictions. Detailed guidance is then retained in VPGA 10, with the emphasis on qualitative rather than quantitative comment. The fundamental point here is to ensure that – from the client's perspective – the report is not misleading.

VPS 4

There was some questioning over whether the content of VPS 4 was truly a standard – despite it linking with IVS 104 – on the basis that there was an absence of positive 'actions'. This has been addressed by making clear the requirements at the outset, the most fundamental of which is that the **valuer must ensure that the basis of value adopted is appropriate for, and consistent with, the purpose of the valuation**. Some other detailed comments on the various bases were directed more at the content of IVS 104, but a suggestion for further clarification of investment value has been taken up. Also, a suggestion that a cross-reference to the 'conceptual framework' for market value in the IVS be inserted has been adopted, given the importance of a proper understanding of this. An additional **cautionary note concerning fair value for inclusion in IFRS-compliant financial statements has been added**. Obviously, by no means all financial statements fall to be prepared under IFRS – the particular reporting standards relevant to individual valuation assignments must always be carefully observed.

An opportunity has been taken to **refine the text on assumptions and special assumptions** with the definition of the former now reproduced in full. Some reservations were expressed about how helpful or otherwise the content of paragraph 9.4 is: but the emphasis here is on the word 'may', as it does not follow that a special assumption is necessarily needed or appropriate – some matters may be covered adequately by a factual statement or at most by a (non-special) assumption. As there was limited overall comment on the subject, it has been decided to retain the material but keep it under review. The **content in section 11** on **projected value has been refined**, among other things, **to recognise that both types of assumption may arise in such cases**, albeit that **special assumptions** made will be of **particular importance regarding the valuation outcome and a client's understanding of it.**

The position regarding 'forced sales' was also queried in one of the consultation responses. The relevant part of VPS 4 (paragraph 10.8) states that 'although advice may be given on the likely realisation in forced sale circumstances, the term is a description of the situation under which the sale takes place, and so it must not be used as a basis of value.' This echoes IVS 104 at Section 170, where it is explicit that '**forced sale' is a 'premise of value' not a 'basis of value'** – thus at the end of paragraph 170.1 it says: '**The price that a seller will accept in a forced sale will reflect its particular circumstances, rather than those of the hypothetical willing seller in the Market Value definition**. A "forced sale" is a description of the situation under which the exchange takes place, not a distinct basis of value'. In short, an RICS member can provide 'forced sale' advice but must be very careful about the terms in which it is reported.

VPS 5

The new VPS 5 – which links to **IVS 105** – resulted in a number of comments about RICS changing its longstanding position from one of not prescribing valuation approaches and methods to one that does. This is not the case, and the key principles highlighted in bold at the outset of this section are intended to restate and reinforce the established RICS position that it is valuers who have the primary responsibility here. Indeed, as IVS 105 itself says: '**The goal in selecting valuation approaches and methods for an asset is to find the most appropriate method under the particular circumstances**.' While on occasions a particular approach or method may be specified in jurisdictional legislation, which then becomes mandatory, otherwise there is no prescription here. Indeed, RICS would be most concerned to find that members were not properly exercising their own judgment in relation to individual valuation assignments.

Minor edits have been undertaken to ensure the various references are to method(s) rather than methodology.

Introduction to Part 5: Valuation Applications

The **Introduction has been amplified both to clarify the status of the VPGAs and to include a list of the IVS Asset Standards, to which cross-references are made in the VPGAs**. There are **two additional VPGAs** by comparison with the Consultation Draft, namely:

- **VPGA 9 – Identification of portfolios, collections and groups of properties**
- **VPGA 10 – Matters that may give rise to material valuation uncertainty**

The reasons for including these have been explained above.

VPGA 1

Contrasting views were received on whether this VPGA should be dropped or indeed expanded. It has been decided to retain it on the basis that it is a significant area of activity for at least some RICS members, and the importance of being alert to, and possessing sufficient knowledge of, the relevant reporting standards – against a global background of continuing convergence between a number of jurisdictional standards and IFRS – when undertaking this work cannot be overstated.

VPGA 2

Some minor edits have been undertaken to ensure consistency and clarity as between advisory material and signposting cross-references to mandatory requirements.

VPGA 3, 5, 6 and 7

Some minor edits have been undertaken to accommodate various detailed drafting points raised.

VPGA 8

Some observers felt that this lacked clarity and was rather a miscellaneous collection of matters, notwithstanding the fact that it had substantially been brought forward from the 2014 edition of the Red Book. While preserving the general coverage, the opportunity has been taken to improve the overall presentation and some of the detailed content. It is hoped that this will prove more useful.

Miscellaneous matters

A number of issues were raised not necessarily bearing directly on the Consultation Draft text, for example, in one case a desire to see the inclusion of valuation templates. Such comments have been noted, and may well prove relevant to Red Book national supplements as they are issued or updated, but since these comments are not reflected in the revised text of the Global Standards, they are not addressed further here.