International Valuation Standards Council (IVSC)

Exposure Draft

Development Property

Response of the
Royal Institution of Chartered Surveyors (RICS)

Contact:
Alexander Aronsohn FRICS
RICS Director of Technical International Standards
aaronsohn@rics.org

Ben Elder *FRICS*
RICS Global Head of Valuation
belder@rics.org

Royal Institution of Chartered Surveyors
Parliament Square
London SW1P 3AD
United Kingdom
t +44 (0)247 686 8555
f +44 (0)207 334 3811
e contactrics@rics.org
rics.org

Introduction

The Royal Institution of Chartered Surveyors (RICS) has noted the publication of the Exposure Draft – Development Property – produced by the International Valuation Standards Council (IVSC) in January 2014 and welcomes the opportunity to comment.

About RICS

RICS is the global leading organisation for professionals in real estate, land, construction and related environmental issues as well as working in the personal property and business assets sectors.

Over 120,000 RICS members, who are Chartered Surveyors, exist globally and operate out of 146 countries, supported by an extensive network of regional offices (detailed on our website) located in every continent. RICS Headquarters is based in London and our international work is supported by a network of regional offices and national associations.

RICS members play a vital role throughout the entire asset life cycle – from initial inspection and measurement, development through to investment in, and the use of physical structures and other assets, as well as financial and business interests. In the valuation field our members' expertise covers a very wide range of disciplines, including business valuation. We also provide impartial advice to governments, policymakers and non-Government organisations.

RICS is an independent professional body, which was established in 1868 and has a UK Royal Charter. It is committed to setting and upholding the highest standards of excellence and integrity, providing impartial and authoritative advice on key land and asset issues affecting businesses and society.

RICS is a regulator of both its individual members and firms enabling it to maintain the highest standards and providing the basis for unparalleled client confidence in the sector. This regulation includes a specific focus on valuation via Valuer Registration.

As well as technical standards there are also rules of conduct for members and rules for the conduct of business for firms. These rules are coupled with ethical standards for all members.

RICS and Valuation Standards

A significant proportion of our members are involved in valuation practice on all manner of assets. The first RICS Valuation Standards publication was produced in 1976 and the current standards are the "RICS Valuation – Professional Standards" effective from 1st January 2014. The standards are commonly known as "the Red Book" and contain mandatory rules and best practice guidance for valuations of real estate and other assets.

RICS adopts the International Valuation Standards (IVS) 2013. The adoption of IVS in the Red book provides an implementation and practice framework for the application of IVS globally, ensuring that RICS members follow consistent methodologies throughout the world.

The Red Book is mandatory for all RICS members and regulated firms worldwide when carrying out Red Book specific valuations. It is also widely referred to by non-RICS valuers.

The global section of the Red Book comprises a broad ethical framework which can be applied to valuations of any asset type in any jurisdiction, in harmony with national legislation. They comprise a framework for the following:

- VPS1 – Minimum terms of engagement;
- VPS2 – Inspections and investigations;
- VPS3 – Valuation reports;
- VPS4 – Bases of value, assumptions and special assumptions.

More specifically the standards relating to compliance with standards and practice statements where a written valuation is provided and ethics, competency, objectivity and disclosures are set out in Professional Standards PS1 and PS2.

The global standards are accompanied by detailed national standards.

For more information please visit http://www.ricsvaluation.org/

29 April 2014

Our Ref: BE/AA/EDR3

International Valuation Standards Council
1 King Street
London
EC2V 8AU

Dear Sirs

Re: RICS OBSERVATIONS ON THE EXPOSURE DRAFT ON DEVELOPMENT PROPERTY

The IVSC Discussion Paper (December 2012) to which reference is made reflected the concerns that IVSC themselves had with the current IVS 233 Investment Property under Construction and with which the RICS had also raised issues. To that extent this Exposure Draft is welcomed.

However the RICS still consider that the proposed paper - intended to provide "more broadly based guidance on the valuation of any type of real property that is either in the course of construction or where construction is contemplated, i.e. 'development property' " - is still an anomaly and beyond the remit of the IVSC as setter of international standards. The RICS considers it to be the responsibility of Valuation Professional Organisations to provide "supporting information and guidance" to their members on the detailed implementation of international standards.

However the RICS response solely on the Exposure Draft as published is as follows;

1. Do you agree with the Board's proposal to move all material in the [international valuation] standards specific to financial reporting to IVS 300?

RICS agrees that all standards material specific to financial reporting should be grouped together within IVS 300. As noted above, we do not however consider that the full content of IVS 233, or an expansion of it, has a place in that grouping.

2. Do you agree with the Board's view that the valuation techniques described in the commentary to the current IVS 233 are applicable to all types of development property, not just investment property as defined in IFRS?

The RICS agrees that the various considerations to be taken into account when valuing all types of development property are not limited to those under construction, nor to investment property. However the RICS does not consider that valuation approaches (which is the wording used in the current IVS 233) or valuation techniques (the wording used in this consultation question) should form part of an IVS. The standards are effectively set out in the Requirements section of the current IVS 233. It does not require expansion beyond that point, and indeed it is important to bear in mind that there are disparate regulatory and other factors that valuation practitioners are required to consider worldwide, which are better addressed by the relevant Valuation Professional Organisations.

3. Do you agree with the scope [of the proposed Technical Information Paper] as described? If not, please explain any additional matters that you believe should be added to the scope or matters currently included that you believe should be excluded

The scope, as previously identified in IVS 233, was limited primarily to stating the extent of the investigations and the source of the information together with the agreeing and stating of any special assumptions. The proposed scope set out herein is much wider extending to "guidance on appropriate valuation procedures, approaches and methods" which the RICS does not believe is appropriate and should be excluded.

In more detail:

- Whilst noting the stated objectives within the IVSC Investment Property Project, the RICS believes that this proposed guidance is too much directed to practical valuation issues, including valuation methods (see paragraph 4 of the draft), rather than focussing on higher level principles and on direct interpretation of international valuation standards. Indeed in certain respects the content is not dissimilar to material used in first year undergraduate courses.

- RICS also believes it is wrong for IVSC to advance definitions of valuation terms other than those included in the IVS Definitions section of the International Valuation Standards. If retained, paragraph 5 should be rewritten to make clear that the terms included within that section are explained in terms of their use within the document, and are not defined terms as such

4. Please indicate if there are any items on [the] list [in paragraph 7] with which you disagree or any additional matters you believe should be included

As the paragraph 7 list is deliberately non-exhaustive, it is purely a matter of judgement as to how much is included and at what level of detail – and there is a risk in referring to "typical" when seeking to cover all jurisdictions. But if a list is to be retained, It may be thought that a reference to flooding risk could be appropriate – as much an environmental as a geotechnical issue.

5. Do you agree [with paragraph 15, which suggests that all three valuation approaches identified in the IVS Framework can be applied to development property]? If not, please explain why

Depending on the nature of the development, or refurbishment, and the stage of the works at the date of valuation all or any of the three could be applied to some extent but convention differs in different jurisdictions and the validity of the valuation advice may suffer if wrongly applied or misinterpreted.

Furthermore the dedication of paragraphs 16-18 to the market approach and 19–23 to the income approach, which leads into a discussion on the residual method, and 29–31 to the cost approach, underlines that there are more than three approaches, and indeed there are others which would need to be expanded upon if the paper were to have global coverage. The bottom line is that the valuation approach to be used must always be that which is most appropriate to the particular facts and circumstances, and it might be better if paragraph 15 brought this out.

Overall the RICS considers that the explanation of these approaches is better left to the Valuation Professional Organisations operating in the various jurisdictions worldwide to cover.

6. Do you consider the caution provided here [in paragraphs 20-22] is sufficiently detailed or do you consider further guidance is required?

We would reiterate our view that IVSC should not be attempting to provide such guidance itself, which would be better addressed by the Valuation Professional Organisations, technical publishers and the academic world in more focused and in depth publications.

Inter alia, we would point out seemingly conflicting statements about the approach to the valuation of the “completed property” in paragraphs 23 and 24(a) support our view that the inclusion of these sections would be counter-productive.

7. Do you consider that there any typical inputs that are not referenced [in paragraph 24] but should be included or items included that would not typically be used? If yes, please identify the input and the reasons for inclusion or exclusion

The attempt to “cover all angles” in the paper does lead to some potential difficulties e.g. the lead in to paragraph 24, which we consider may refer to a DCF type evaluation of worth (or investment value), rather than Market Value could be confusing.

Under Finance Costs the wording, which is unchanged, is not plain and, if this section is retained, could benefit from revisiting to ensure it is interpreted consistently.

The Consultants Fees section requires further explanation to ensure it is understood these could relate to fees to be incurred at any stage in the development.

Again the concepts of stabilised occupancy and income in the Buyers Profit and Risk section (we would query why specifically buyers?) should be revisited if this section is to remain as it has little place in the wider, i.e. beyond financial accounting, consideration of residual land values.

8. Do you consider that there are any other methods for determining the interest rate that should be included [in paragraph 25]? If so, please explain these

The approach set out in paragraph 25 is purely relating to the discounted cash flow methodology which is primarily utilised in the calculation of worth (or Investment value) not Market Value. It focuses on the discount rate, not the interest rate that might be utilised in a residual appraisal which is determined by reference to interest rates and opportunity cost.

9. Do you agree with [the] list [in paragraph 34 of matters that should be included in a valuation report]? If not, please identify any additional matters you would like to see included or matters that are included that you think should be excluded, with supporting reasons

Given the diversity of circumstances, it is very difficult to generalise in terms of the matters properly to be included in individual valuation reports. Provided IVS 103 and IVS 230 are followed (and in the case of RICS members, additional matters covered in the Red Book) and that the client's attention is expressly drawn (in the Terms of Engagement/Scope of Work and the Valuation Report) to matters considered to be significant in the particular case, the reporting of values for development property should not be seen as following different principles or conventions. The matters covered in paragraph 34 are likely to feature but there is a risk in implying that this may be a comprehensive list.

10. Do you agree that this type of disclosure [i.e. a sensitivity analysis, as referred to in paragraph 35] is helpful and should be encouraged wherever appropriate?

Yes, provided the sensitivity analysis is accompanied by a suitably detailed and plain interpretive text to enable the advice to be appropriately applied. One might add that sensitivity analysis is unhelpful in most secured lending situations, as the presentation of various permutations of possible "value" is often misunderstood or misinterpreted.

Yours faithfully

Ben Elder BA BSc FRICS ACIArb
Global Director of Valuation
RICS Professional Groups

T +44 (0) 20 7695 1695
F +44 (0) 20 7334 3712
E belder@rics.org
www.rics.org