International Valuation Standards Council (IVSC)

Consultation Paper

IVSC EXPOSURE DRAFTS FOR IVS 2017 OF 7 APRIL 2016

These observations relate to the sections of the International Valuation Standards (IVS) 2017 issued for consultation by IVSC on 7 April 2016, namely:

- IVS Introduction and Framework
- IVS 104 Bases of Value
- IVS 105 Valuation Approaches and Methods
- IVS 210 Intangible Assets

Response of the
Royal Institution of Chartered Surveyors (RICS)

Contact:

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Tuesday, 28 June 2016
Dear Sirs,

I am pleased to attach herewith the RICS’s formal feedback on the IVSC Consultation Exposure Drafts for IVS 2017 of April 2016 covering:
- IVS Introduction and Framework
- IVS 104 Bases of Value
- IVS 105 Valuation Approaches and Methods
- IVS 210 Intangible Assets

We welcome the opportunity to comment on the exposure drafts and wish to complement the endeavors of the Standards Board in producing the documentation.

Introduction

The Royal Institution of Chartered Surveyors (RICS) has noted the publication of the Consultation Paper – Structure and Scope of the International Valuation Standards – produced by the International Valuation Standards Council (IVSC) in July 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/
RICS OBSERVATIONS ON IVSC EXPOSURE DRAFTS FOR IVS 2017 OF 7 APRIL 2016

Preface

These observations relate to the sections of the International Valuation Standards (IVS) 2017 issued for consultation by IVSC on 7 April 2016, namely:

- IVS Introduction and Framework
- IVS 104 Bases of Value
- IVS 105 Valuation Approaches and Methods
- IVS 210 Intangible Assets

RICS will respond separately in relation to the further exposure drafts released on 2 June 2016 with a response deadline of 31 August 2016.

Overall, RICS acknowledges the considerable effort that has gone into the process of review of IVS 2013 and the development of the current proposals for IVS 2017. The conclusion reached that “IVS 2017 should only include mandatory standards and that the provision of information or guidance (is) outside the remit of the IVSC” (first bullet of first paragraph on page 4 of IVS 2017 Introduction and Framework) is welcomed, as is IVSC’s decision to remove the Application chapters and rescind the Technical Information Papers (TIPs) as IVS 2017 goes live.

RICS responses to the questions expressly posed in the 7 April Consultation Drafts are set out in detail below, together with some additional comments and suggestions. Necessarily the comments focus on the points where revision or refinement is seen as desirable. This should not detract from the fact that – as a long term contributor to, and committed adopter of, IVS - RICS is strongly supportive of the bulk of the content and the clarity of the overall structure.

RICS would particularly highlight the following two key issues where discussion with the VPOs is seen as essential before the text can be satisfactorily finalised:

- The definition of (professional) “valuer”, where the versions proposed by IVSC in the separate but parallel IVS and International Professional Standards (IPS) Consultation Drafts differ
- The rationale for the adoption of two new bases of value proposed by IVSC – “Liquidation Value” and “Replacement Value” – and especially the associated definitions, which RICS believe have certain shortcomings in their present form, and require a sharpening of focus

IVS 2017 Introduction and Framework

- Comments on specific questions posed:

Qu 1: In IVS 2013, all substantive portions of the standards were labelled as “commentary” (except for scope and effective date). This label seems to have created some confusion amongst stakeholders as to whether the standards were
mandatory. The Board's position is that all aspects of IVS 2017 should be mandatory and this exposure draft has removed the "commentary" label for clarity. Do you agree with the removal of the commentary label?

IVSC's objective to focus IVS 2017 content on mandatory standards – removing information and guidance material - is welcomed. However, in some instances, noted in relation to the individual standards concerned, further editing is considered necessary to achieve this objective fully. Thus whilst the standards must necessarily be set in context, as the revised IVS Framework explains ("Certain aspects of the standards do not direct or mandate any particular course of action, but provide fundamental principles and concepts that must be considered in undertaking a valuation" – page 6 of the Consultation Draft) there is some material remaining which is more discursive. The clarity of the standards would be enhanced if this were better differentiated.

**Qu 2:** Do you agree with the Board's decision to remove the section on Bases of Value from the IVS Framework and produce a single chapter on Bases of Value in order to clarify the mandatory nature of this section and to avoid repeating certain guidance throughout the IVS? If not, why?

A standard expressly covering Bases of Value is particularly useful for valuation providers, as well as for clients/valuation users, and so is welcomed. RICS does however have some observations on the content of the new IVS 104 _Bases of Value_, which are set out later below.

**Qu 3:** Do you agree with the Board's decision to remove the section on Valuation Approaches from the IVS Framework and produce a single chapter on valuation approaches and methodologies in order to clarify the mandatory nature of this section and to avoid repeating certain guidance throughout the IVS? If not, why?

Whilst there is again some benefit to valuation providers in having the material assembled into a self-contained standard, once more RICS has some observations on the detail of the new IVS 105 _Valuation Approaches and Methods_ – set out later below – including some concerns about the inclusion of non-mandatory material relating solely to certain individual jurisdictions.

**Qu 4:** Do you agree with the IVS definition of Exceptions and Departures? If not, why?

The explicit recognition of the need – as circumstances may dictate - for Exceptions (eg where standards other than IVS have to be complied with) and Departures (where there are legislative, regulatory etc overrides) is useful. It is assumed that
IVSC would expect VPOs to further characterise “inappropriate” in relation to the proposed definition of Exception, and “authoritative requirements” in relation to the proposed definition of Departures (see also further comment on paragraph 60.4 below).

- **Additional observations**

  o Page 4 and paragraph 30.1: The proposed definition of “Valuer” refers only to “necessary” qualifications and omits any reference to professional and technical skills (see for example IVS 2013 Framework paragraph 4) or membership of a VPO. It is not clear how “necessary” would be judged and there is a need to link the definition more closely and objectively with the paragraphs that follow. Additionally, the definition of a “professional valuer” in the International Professional Standards (IPS) Draft issued for consultation by IVSC on 31 March 2016 is expressed in different terms (**paragraph 22 of the IPS Framework**). As a link is made with the IPS in the second sentence of the second paragraph of the IVS Introduction and Framework Draft at page 6, it is essential that a common definition of a professional valuer is adopted. It is suggested that IVSC work with the VPOs to arrive at a consistent definition of universal application.

  o Page 6: Second paragraph, first sentence: The circularity in the present draft could be overcome by deleting “to assist the consistent interpretation of those principles” and substituting “which promote transparency and consistency in valuation practice”.

  o Page 9: Paragraph 60.4: It is not clear whether “authoritative requirements” would cover the situation where a departure is pursuant to requirements of a shareholder agreement.

**IVS 104 Bases of Value**

- **Comments on specific questions posed:**

  **Qu 1:** Do you agree that valuers should be responsible for choosing the appropriate basis (or bases) of value according to the terms and purpose of the valuation assignment, and that the basis of value may not be one defined by the IVSC? If not, why?

  The use of the word “sole” in relation to the valuer's responsibility to “choose” the relevant basis (or bases) of value is wrong and should be deleted. Whilst in many instances the valuer will have prime responsibility for ensuring that the basis of value
adopted is consistent with the terms and purpose of the valuation assignment, in other cases the basis of value will be pre-determined by the client and/or by the particular purpose or context eg a request for a valuation for reporting in accordance with IFRS 13. The basis may even be prescribed by regulation or statute, leaving the valuer no discretion whatever, as in effect is recognised in the wording of paragraph 10.2 of the IVS 104 draft. What is essential is that there should be clarity on the part of both provider and client concerning the basis of value and key assumptions insofar as they may impact on the reported value, and these should be embodied in the terms of engagement for the task.

On the second limb of this question, clearly there will be instances where a basis of value not defined by IVSC is appropriate, indeed sometimes mandatory. It is essential that this need for flexibility is recognised within IVS.

Qu 2: Prior versions of international valuation standards included “Special Value” as a separate and distinct basis of value. The Board generally believes that valuers seldom perform valuations using Special Value as a distinct basis of value. Rather, valuations are typically performed using another basis of value predicated on certain hypothetical assumptions (“special assumptions”) or a specific purchaser (resulting in synergistic value). Do you agree with the removal of Special Value as a separate and distinct basis of value? If not, please describe the circumstances in which you use Special Value as a distinct basis of value?

The observation that valuers would not perform valuations using Special Value as a distinct [sic] basis of value is sound, but there will be instances where – in relation to a particular asset - a special purchaser can be identified and, if so, there is an obligation on valuers to highlight the fact and to draw the client’s attention to it. Since market value excludes such element, the additional bid that might be made by this known potential buyer must be identified and reported appropriately ie separately from the market value. The drafting at paragraph 70.1 and paragraph 70.2 does not refer to this important responsibility.

Qu 3: IVSC has retitled the previously defined Fair Value as Equitable Value in order to avoid confusion with other definitions of Fair Value. Do you agree with this change, if not why not?

The use of a different title to remove the potential confusion with IFRS Fair Value is welcomed.
Qu 4: Liquidation Value has been added as an additional basis of value. Do you agree with its inclusion within IVS 2017 and are you in accordance with the definition used? If not, why not?

Within the proposed definition the possibility of assuming either an orderly or disorderly (a “forced transaction”) disposal raises doubts as to whether this is a single prescribed basis of value, or in some instances a situation where the starting point might be Market Value (modified by the addition of some extensive assumptions or special assumptions – which must be realistic) or Investment Value. Furthermore, the reference to “going concern business” suggests that the definition is intended to be of application for the purpose of business valuations rather than necessarily in relation to other forms of asset - if this is what IVSC intend, then the drafting could be made clearer.

These doubts are reinforced by the cross-reference in the proposed definition to Sections 170 and 180, where a forced sale (forced transaction) is expressly not recognised as a basis of value. As the last sentence of paragraph 180.1 explains: “A ‘forced sale’ is a description of the situation under which the exchange takes place, not a distinct basis of value”.

It would be helpful if IVSC could engage in discussion with the VPOs to ensure that the intention behind this new addition is fully understood and can then be suitably realised.

Qu 5: Replacement Value has been added as an additional basis of value. Do you agree with its inclusion within IVS 2017 and are you in accordance with the definition used? If not, why not?

Again, inclusion within IVS 2017 would be premature. The Basis of Conclusions accompanying the Consultation Draft states “it is common market practice for most valuation instructions for secured lending purposes to also request the provision of an Estimated Replacement Cost/Insurance Value for insurance purposes”. However, the provision of a replacement (or, particularly in relation to real estate, reinstatement) cost figure for the purposes of insurance often requires no valuation input or judgement at all. Therefore the proposal to use the term “Replacement Value”, presenting it on the same footing as any other basis of value, is misleading.

It is suggested that IVSC devotes additional time, in liaison with the VPOs, to fuller analysis and consideration of the issues – including their relevance to different types
or classes of asset – in order to differentiate and distinguish clearly between replacement cost, reinstatement cost and reproduction cost, all of which on occasions can be loosely referred to as replacement “value”. It is noted that replacement cost and reproduction cost feature as terms in the accompanying draft IVS 105, but at present without formal definition.

Qu 6.: Are there other bases of value defined by other entities/organizations that should be mentioned in IVS 104? Which ones? Why?

Not at this stage.

• Additional observations

  o Page 7: Paragraph 20.1 (b) Other bases of value (non-exhaustive list): Whilst there is a clear case for the inclusion of item (i) IFRS Fair Value, since it is an international financial reporting standard, the inclusion of the remaining items is questionable. In particular, inclusion of (iii) and (iv), which are purely national, federal or state standards, and are given more extensive treatment in paragraphs 120.1-2 and 130.1-2, is wholly inappropriate in International Valuation Standards, where local jurisdictional content – whether for illustration or otherwise - has no place. Additionally, it is not clear why the important observation at paragraph 39 of the existing 2013 IVS Framework re the equivalence of IFRS Fair Value to IVSC Market Value is not repeated here – this could usefully be added at paragraph 100.1.

  o Page 6: Paragraph 10.1: A basis of value will not normally describe the unit of account for a valuation (none of the IVS-defined bases do) – this is usually a matter of fact to be discussed and agreed between valuation provider and client.

  o Page 8: Paragraph 20.2: The statement is incorrect. It is, as explained above, in many cases not solely (or not even) the valuer’s responsibility to “choose” the relevant basis (or bases) of value. It will often be dictated by the circumstances or context, and may indeed even be defined by statutory or regulatory requirement.

  o Page 10: It is not clear why paragraph 31 in the existing 2013 IVS Framework has been dropped – being clear about the market in which the hypothetical transaction is presumed to take place is of fundamental importance.

  o Page 11: Paragraph 50.2: For the sake of completeness “....or disadvantages......incurred by....” should be added to the second sentence, as a counterbalance to the first.
Page 18: Paragraph 210.4 (b): A very small typo – “that a” is repeated twice
Page 18: It is also not clear why paragraph 35 in the existing 2013 IVS Framework has been dropped, as in the context of market value paragraph 220.2 could lead to ambiguity. In any event, paragraph 220.1 could usefully make some explicit reference to IVSC-defined bases.

IVS 105 Valuation Approaches and Methods
• Comments on specific questions posed:

Qu 1: Do you agree that when selecting appropriate valuation approaches and methods a valuer should consider the following?
• the appropriate bases of value, determined by the terms and purpose of the valuation assignment,
• the respective strengths and weaknesses of the possible valuation approaches and methods,
• the appropriateness of each method in view of the nature of the asset, and the approaches or methods used by participants in the relevant market,
• the availability of reliable information needed to apply the method(s).
If not, why? What considerations would you add to or remove from this list?

No exception is taken to this list, though of course there may be other considerations to take into account.

Qu 2: Under each valuation approach, this exposure draft includes criteria for when the approach should be used. Do you agree with the criteria presented under each approach? If no, what changes would you make? Why?

A material concern here is that a significant amount of the accompanying material constitutes guidance – indeed the Introduction to IVS 105 expressly makes reference to the chapter including “discussion” material. It is clearly not consistent with the statement that “the [IVSC Standards] Board’s position is that all aspects of IVS 2017 should be mandatory.” To address this problem and assist users, it would be better if the draft were reworked to draw out the fundamental principles more clearly, perhaps along the lines of the 2013 IVS Framework, with the supporting guidance or (to adopt the Basis of Conclusions description) “guidelines”, including the “how to” aspects appropriately subordinated. Presenting all the material as a continuous run, as the draft currently does, leaves the individual reader to judge the division and balance between the two. This is not to say that the explanatory material may not be welcome in certain markets, but it is clearly not a standard per se.
An additional concern is that the material is presented as though it is of general application, but in places includes detail relevant to particular types or classes of asset without making the transition from the general to the particular sufficiently clear. And given the level of detail otherwise included in the draft, it is not clear why there are certain omissions — thus capitalisation of future income streams where both rents and yields are derived from market evidence eg as commonly used for real estate valuations, is not referred to under either the heading “Market Approach” or the heading “Income Approach”.

**Qu 3:** Are there areas of this chapter that you feel should be expanded upon in future board projects (e.g. discount rates, discounts/premiums, etc.)?

The draft is already too detailed to be correctly described simply as a standard. Great caution should therefore be exercised in adding to its length or increasing the lower level detail.

- **Additional observations**
  
  o Page 7: Paragraph 10.6. The drafting is unsatisfactory. It is not always the case that one approach or method of valuation takes clear precedence over another. The valuer must always weigh the evidence, analyse inputs, evaluate outputs and review preliminary conclusions as appropriate to arrive at an overall opinion.
  
  o Page 7: Paragraph 10.8: the use here of the term “appraiser” rather than “valuer” is not explained — is there intended to be some distinction? Additionally there may be differing interpretations as to when a market is, or is not, “active” — does this require some further articulation?
  
  o Page 8: Paragraph 20.3: The circumstances listed could well lead to valuation certainty being affected, on which a commentary in the valuation report may be necessary
  
  o Page 9: Paragraph 30.4: The valuation of financial instruments is generally far more complicated than the sentence here implies — overall the key point is contained in the final sentence
  
  o Page 9: Paragraph 30.5: The time frame over which transactions are considered is also important
  
  o Page 12: Paragraph 30.14: It is not clear why “material physical characteristics” would be important in this regard
  
  o Page 9: Paragraph 30.7 et seq: A similar observation to that immediately above can be made in relation to the unexplained introduction of the word “professional” in place of valuer
IVS 210 Intangible Assets

- Comments on specific questions posed:

**Qu 1:** In IVS 2013, all substantive portions of IVS 210 Intangible Assets were labelled as “commentary” (except for scope and effective date). This label seems to have created some confusion amongst stakeholders as to whether the standard was mandatory. The Board’s position is that all aspects of IVS 2017 should be mandatory and this exposure draft has removed the “commentary” label for clarity. Do you agree with the removal of the commentary label?

The IVSC’s standpoint is logical ie that, so far as possible, a standard should be mandatory in its entirety, but – as the Introduction explains – the present draft expressly includes “discussion” material which clearly is akin to guidance or commentary, and is also selective (see for example paragraph 50.1). As noted above, to address this problem, rather than describing IVS 210 as mandatory in its entirety, it would be better to recognise explicitly that it contains standards, associated best or good practice to which valuers should adhere unless there is an identifiable and justifiable reason not to do so, and other purely explanatory or descriptive material (eg sections 150 and 160). Some reworking of the text would be needed to achieve this, but would be welcomed as an aid to clarity. It could be said that Paragraph 10.1 already points to the need for this, as the emphasis there is on principles.

**Qu 2:** Do you agree with the decision to incorporate relevant portions of TIP 3 into IVS 210 and to eliminate TIP 3 as a standalone document? Are there any other elements of TIP 3 that you believe should be incorporated into IVS 210?

It is agreed that IVSC’s concentration on standards is the right priority, leaving detailed guidance on valuation practice for VPOs. The withdrawal of TIP 3 is also endorsed. But as noted in the response to Qu 1 above, part of the material drawn from TIP 3 now included in this draft is not a standard, but supporting guidance or explanation. Some clearer differentiation between the two elements would be helpful to users.

**Qu 3:** In addition to the contents of IVS 105, this exposure draft includes criteria that should be used by an appraiser [sic] in selecting an appropriate valuation approach.
and method for the valuation of intangible assets. Do you agree with the criteria presented under each approach? If no, what changes would you make? Why?

This question is not wholly understood. The focus in the draft appears to be more on the execution of the valuation task than on the decision-making process for adopting a particular approach and/or method of valuation.

Qu 4: The Board believes that the standard presented in this exposure draft can be applied in the valuation of intangible assets regardless of the purpose of the valuation (financial reporting, tax, transactions, litigation, etc.). Do you agree? If not, for what purpose(s) do you not believe this standard can be applied? Why?

No immediate observations

• Additional observations:

  o The reference in the 2013 IVS Framework (at paragraph C11) to goodwill having different definitions (eg under certain financial reporting or tax regimes) has been dropped, but it is not clear why
  o Page 5: Paragraph 20.3: The opening sentence should be amended to read: “There are many types of intangible asset, but......”
  o Page 5: Paragraph 20.3 (b): It is not clear why “or supplier-related” has been dropped (see IVS 2013 existing IVS 210 paragraph C5)
  o Page 5: Paragraph 20.3 (e): Valuing technology assets involves certain special considerations – perhaps some cautionary note concerning this needs to be inserted
  o Page 5: To follow paragraph 20.3: It may also be advisable to insert a cautionary note to the effect that a “brand” typically comprises a combination of intangible assets, including many of those listed
  o Page 5: Paragraph 20.4: This adds nothing and could be deleted
  o Page 7: Paragraph 20.10: Reference to the valuer having “sole” responsibility is not correct – there will be occasions where a discussion with the client is essential to ensure that the assets (or liabilities) involved are correctly identified and correctly grouped
  o Page 12: Paragraph 70.4: The term “appraiser” is used rather than “valuer” without any obvious rationale. Also paragraphs 70.5 and 70.6 appear to be intended as indents to paragraph 70.4, rather than being separate
Thank you again for the opportunity to comment on the draft documentation

Yours faithfully

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