



## INTERNATIONAL VALUATION STANDARDS COUNCIL – FEEDBACK FORM

### Royal Institution of Chartered Surveyors (RICS) response to the IVS 500 Financial Instruments Exposure Draft

7 May 2021

#### Introduction

- The Royal Institution of Chartered Surveyors (RICS) welcomes the opportunity to respond to the IVS 500 Financial Instruments Exposure Draft. Some of the questions principally relate to matters beyond the scope of RICS's main specialisms of tangible assets valuation, business valuation and matters related to the built environment. We have therefore limited our response to principles covered by current RICS standards and our members core work functions.
- RICS members and firms are involved with the valuation and management of assets globally, which may include funds, trusts and other investment vehicles, principally related to real estate. However, this response does not attempt expert commentary on specific financial instrument and regulatory considerations outside RICS specialisms. RICS recognises the link between financial instruments and other core valuation functions.
- RICS supports a successful and well-functioning real estate and business market and by extension, investment in real estate and business. We believe that this aligns with our principle objective of acting consistently in the public interest. To support a well-functioning market RICS welcomes the development of further relevant standards.
- RICS produces the Global Standards - Valuation "Red Book" (hereafter referred to as RICS Global Red Book, which provides a professional framework for the valuation process, giving reassurance to valuation stakeholders including investors, regulators and government. The RICS Global Red Book has additional national supplements, which may refer to matters directly and indirectly related to financial instruments such as, for example, the valuation of authorised funds, collective investment schemes, unregulated property unit trusts and other investment classes. The supplements also include coverage of valuation relating to

financial reporting and taxation relevant to particular jurisdictions. The RICS Global Red Book also contains specific standards related to business valuation and we produce guidance on the valuation of intangible assets. Within our standards are mechanisms to deal with various market scenarios, including different valuation purposes and bases. Our standards are produced on an agile basis, regularly updated to consider relevant market and regulatory impacts.

- **Given that RICS standards incorporate IVS (including the current version of IVS 500), we consider it of utmost importance that principles and core content of the standards align.** Furthermore, all of our global standards must be capable of regulation and assurance and the basis for doing so accountable with our membership and stakeholders. Given the relationship between IVS and the RICS Global Red Book, we welcome your further engagement on this process, including advance notice of the final content.
- RICS is currently subject to two reviews of its professional output and delivery. The first is an Independent Review of Real Estate Investment Valuation where an independent chair and expert advisory group are to provide recommendations to the RICS Standards and Regulatory Board later this year. The second review, “Defining our Future” is being undertaken by RICS Governing Council and is looking at the role and scope of RICS into the future. Each of these reviews is global, high profile and likely to impact the direction of RICS policy and output. They are referenced here for information.
- Responses to questions are included in the sections below.

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## IVS 500 *Financial Instruments* Feedback Form Questions for Respondents

### IVS 500 *Financial Instruments* Exposure Draft: Objective

The objective of IVS 500 *Financial Instruments* is to establish principles that will enable entities to derive fit-for-purpose valuations of financial instruments in all market conditions and circumstances, and for whatever purpose it is required, including for financial, tax and regulatory reporting.

**Question 1:** Do you agree with the proposed objective? Why or why not? If you agree with only parts of the proposed objectives, please specify what you agree and disagree with. If you disagree with the proposal, please explain what you propose instead and why.

- RICS agrees with the proposed objective as stated above the question, with particular emphasis on the word “principles” as opposed to prescriptive technical guidance. The draft standard refers to “principles and procedures”. The extent and limitations of the procedural element should be elaborated on.
- IVS are global standards (incorporated into the RICS Global Red Book). In RICS’s global operation we have recognised that markets may be at different stages of maturity, have varying underlying infrastructure and are subject to different degrees of regulation and government intervention. This may need to be referred to directly within the proposed amendments to IVS 500, noting the process requirements referenced in the sections below.

**Question 2:** The Exposure Draft is focused on the requirements that have to be met for two elements, Governance and Data, of the proposed standard in order for an entity to arrive at a fit-for-purpose valuation of financial instruments. Do you agree that the requirements are clear, complete and provide adequate guidance to ensure compliance? Why or why not? If you agree with only parts of the requirements, please specify what you agree and disagree with. If you disagree with the requirements, please explain what you propose instead and why. If you think the requirements are incomplete, please explain what you propose should be included and why.

- RICS include commentary on individual parts of the exposure draft in response to the questions below.

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### **IVS 500 *Financial Instruments* Exposure Draft: Scope**

Para 20.1 outlines the scope of application of IVS 500 *Financial Instruments*. In arriving at the proposed scope the FI Board focused on limiting the application of IVS 500 to only those instruments intended by the Board and on ensuring, as far as possible, that all definitions are clear to avoid ambiguity in practice.

In addition, in order to avoid overlaps with extant IVS requirements and the inclusion of instruments that could potentially meet the definition of a financial instrument but are not valued as such within the scope of IVS 500, the FI Board has proposed a number of exceptions to the scope requirements in IVS 500 as outlined in para 20.1 of this Exposure Draft.

**Question 3:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- Detailing the scope of the revised standard, including possible exceptions is welcomed by RICS.
- The impairment exception only refers to GAAP and not say, IFRS.
- If the standard is not just limited to financial, tax or regulatory reporting it may be useful to set out other relevant purposes.

- From an RICS perspective it would be helpful to understand the extent to which financial instruments related to real estate and other illiquid assets are included and any differences there may be.

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### **IVS 500 *Financial Instruments* Exposure Draft: Definitions**

Paras 30.1 to 30.5 provide definitions for the purpose of applying IVS 500 *Financial Instruments*. More specifically they define:

- fit-for-purpose valuations
- financial assets
- financial liabilities; and
- equity instruments

**Question 4:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- RICS has no comment on this section at this time, other than the general comments made in our introduction and in answer to questions setting out the objectives and scope of the draft standard.

In paras 30.6 to 30.8, valuation uncertainty and valuation risk are defined for the purposes of IVS 500 *Financial Instruments*. This Exposure Draft uses valuation risk to set proportionality parameters (para 30.9) that determine the level of effort and the nature and extent of processes and controls needed in order to arrive at a fit-for-purpose valuation of a financial instrument. The objective of the FI Board in outlining the above concept is to enable constituents to evaluate in a consistent manner the extent and rigour of the processes necessary to ensure a fit-for-purpose valuation of financial instruments given the requirement for which it is needed, market conditions and other circumstances prevailing at the valuation date.

**Question 5:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- The scope of the draft standard is noted but given these defined concepts are being introduced to IVS for the first time, it may be worth considering the potential application of these definitions in other areas, and whether their inclusion here creates precedent.
- Valuation risk can also be taken to refer to the probability of a material change in valuation over time (notwithstanding the defined bases of value included elsewhere in IVS).
- The RICS Global Red Book contains specific commentary on uncertainty at VPS3 and VPGA 10, which principally covers “material valuation uncertainty”. The COVID-19 health crisis has seen much testing of these sections, with some success (albeit with the potential for additions and amendments from the lessons learnt).
- RICS has also found valuation uncertainty to be caused by various circumstances such as, for example, material lack of evidence, limitations within the market and in respect of the specific asset (e.g. inability to inspect), pending regulatory or legal changes, inaccessibility of finance and structural and behavioural changes in markets. Further to these criteria, it can therefore be a matter of confidence in the valuation figure as opposed to just the possibility of an alternative, appreciating that this could be regarded as two sides of the same coin.
- RICS has found there to be confusion around valuation uncertainty, material uncertainty and general market conditions. It may be helpful to set out in the draft some context around the relationship between uncertainty and markets.



### **IVS 500 *Financial Instruments* Exposure Draft: Governance**

The Exposure Draft provides guidance on the processes that entities should follow to ensure proper governance around financial instrument valuations. The guidance requires that a valuation process should be:

- systematic
- consistently applied
- economically sound; and
- controlled

In order for the valuation process to meet the above objectives it should require:

- ownership
- accountability
- transparency
- consistency
- review and challenge
- diversity; and
- documentation

**Question 6:** Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- RICS adopts IVS as independent and objective standards. We then apply a valuation framework and set of processes to IVS through RICS Global Red Book and our other standards. Overarching this are our Rules of Conduct for members and firms and

we also have a regulation and assurance function that assures the correct processes and conduct are applied to standards. RICS recognises the place of IVS to consider valuation process and assurance, noting the introduction of the current 2020 IVS, which aims to *“promote transparency and consistency in valuation practice”* and that IVSC also *“promotes leading practice approaches for the conduct and competency of professional valuers”*.

- Whilst IVS has a role to play in terms of commentary related to process and conduct, we believe there is a balance to be struck between general principles and detailed considerations – which adopters of IVS will need to regulate and assure against. Furthermore, there is potential conflict with the wording and interpretation of the proposed IVS governance standards and those of the individual adopter of IVS such as RICS.
- The “diversity” commentary at 50.2.1 states: *“the involvement of multiple disciplines within the valuation process should ensure both that the procedure is free of bias and that the potential impact of information from different data sources is captured in the valuation”*. Whilst it is understood why this would be a useful recommendation in some circumstances – it is something that would then require a regulatory framework around it and need to be fully justifiable in all relevant circumstances globally.
- RICS includes the following statement in our guidance notes which provide good practice advice: *“Guidance notes constitute areas of professional, behavioural competence and/or good practice. RICS recognises that there may be exceptional circumstances in which it is appropriate for a member to depart from these provisions – in such situations RICS may require the member to justify their decisions and actions”* and *“In regulatory or disciplinary proceedings, RICS will take account of relevant guidance notes in deciding whether a member acted professionally, appropriately and with reasonable competence. It is also likely that during any legal proceedings a judge, adjudicator or equivalent will take RICS guidance notes into account. RICS recognises that there may be legislative requirements or regional, national or international standards that take precedence over an RICS guidance note”*. We include this to emphasise the direct link between creating good practice advice and subsequent regulatory and professional requirements for our members.

**INTERNATIONAL VALUATION STANDARDS COUNCIL****IVS 500 Financial Instruments Exposure Draft: Data**

For the purposes of this Exposure Draft, data is considered to be any input to a process undertaken to arrive at a fit-for-purpose valuation. Firstly, the section on data outlines the principles for creating a data taxonomy or dictionary to categorise, assess and control all data that is used in valuations. Secondly, the specific requirements that need to be met for the following data types are outlined:

- internally sourced data
- market data
- transaction data
- model-based/indicative market data
- judgement-based data;
- historical data; and
- performance data

The section further describes the controls necessary for aggregating and managing data in an organisation and how the concept of proportionality applies in determining the requirements concerning the use of data.

**Question 7:** Do you agree with the principles outlined in paras 60.5.1 to 60.5.3 regarding the development of a data taxonomy? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- RICS supports the development of a data taxonomy and the definitions referred to as they support a useful high-level categorisation of data quality. Comments on the balance between a principle based and more prescriptive commentary referred to in question 6 are also relevant to this section.

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**Question 8:** Paras 60.6.2 to 60.6.8 outline the specific requirements for the data-types listed above. Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- RICS in the main supports the definitions and commentary referred to, although note some of the detail goes beyond our main specialisms and therefore a detailed response is not provided. Comments on the balance between a principle based and more prescriptive commentary referred to in question 6 are also relevant to this section.

**Question 9:** Paragraphs 60.7.1 to 60.7.6 outline the principles for controlling and aggregating data across an organisation. Do you agree with these proposals? Why or why not? If you agree with only parts of the proposals, please specify what you agree and disagree with. If you disagree with the proposals, please explain what you propose instead and why.

- RICS in the main supports the definitions and commentary referred to, although note some of the detail goes beyond our main specialisms and therefore a detailed response is not provided. Comments on the balance between a principle based and more prescriptive commentary referred to in question 6 are also relevant to this section.

PLEASE PROVIDE THE FOLLOWING INFORMATION:

Your Details

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Please see the following privacy notice which explains how we use the personal information we collect through your use of our website at [www.ivsc.org](http://www.ivsc.org) ("this website"): [IVSC privacy notice](#)

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