

Preparing a Red Book valuation

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ABSTRACT

The 'RICS Valuation – Global Standards, effective from 31st January 2020', or 'Red Book' as it is colloquially known, sets out the procedures that must be followed by RICS registered valuers when carrying out valuations. Although there is no formal definition of a 'Red Book valuation', it is generally accepted to refer to a valuation in compliance with the current Red Book mandatory requirements. This paper sets out the basic requirements for producing a 'Red Book valuation'. The reader should also refer to the Red Book, both global and national standards, for further details of requirements.

Keywords RICS Valuation – Global Standards, Red Book, RICS registered valuers, Red Book valuation, global and national standards

WHAT IS A 'RED BOOK VALUATION'?

It is important for common standards to be applied to valuations and their reporting, particularly for international investors, to

provide consistent standards and to maintain confidence in the process. A formal valuation report on a property carried out in accordance with the International Valuation Standards (IVS) for, say, an office investment in Singapore should be to the same standards and using the same internationally defined bases as for one in Seattle, Shanghai or Scunthorpe.

The IVS are produced by the International Valuation Standards Council (IVSC), whose members include RICS and most valuation organisations throughout the world and set out the mandatory basic requirements for a valuation in accordance with IVSC requirements, together with guidance on related matters and specific types of valuations. They are regularly updated to reflect current practice and legal requirements.

The RICS uses the IVS as a basis for the Red Book which sets out the application of these standards, reflecting local legal requirements, custom and practice for RICS members.

The Red Book is a procedural manual which 'applies the latest international standards and supplements them with additional requirements and best practice guidance to combine to provide the highest levels of assurance regarding professionalism and quality'.¹

While there is no formally defined term, it is generally accepted that a 'Red Book valuation' can be taken to mean a valuation undertaken in accordance with the standards set out in the Red Book — currently the 'RICS Valuation – Global Standards, effective from 31st January 2020'.

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This paper aims to provide merely a brief outline of the basic mandatory requirements for carrying out a Red Book valuation (PS 1, PS 2, VPS 1–5) and the reader should refer to the requirements in the Red Book for further detail (and any updates since this paper was produced).

The Red Book, particularly the PS and VPS sections, is generic, being applicable to valuations of chattels, plant and machinery, intangible assets, etc. as well as real property. Additional guidance on the valuations for these different categories as well as specific purposes can be found in the VPGA sections such as:

- VPGA 8 Valuation of real property interests;
- VPGA 1 Valuations for financial reporting;
- VPGA 2 Valuations for secured lending.

Further specific requirements and guidance are set out in the relevant National Standards; at present the latest version still relates to the 2017 Red Book,² as the updates for 2020 had not been published at the time of this paper.

The RICS also produces a number of guidance notes and technical articles available to download relating to various types of properties which may be relevant for a particular valuation.

It is a mandatory requirement for valuers undertaking written valuations to comply with sections PS1, PS 2 and VPS 1–5. There are some limited exceptions (nevertheless, even in such cases, the principles of these valuation standards should still be followed wherever practicable) from VPS 1–5 for:³

- Valuations for agency or brokerage work in anticipation of instructions to dispose of, or acquire, one or more assets.⁴ This exception does not cover purchase reports which must still comply with all Red Book requirements;

- Acting or preparing to act as an expert witness;⁵
- Performing statutory functions;⁶
- Valuations solely for internal purposes, without liability, which are not communicated to any third party;⁷
- When valuing expressly in preparation for, or during the course of negotiations or litigation, including where the valuer is acting as advocate.⁸

Since an estimated replacement cost (fire insurance) figure for property is not deemed a ‘written opinion of value’, the sections VPS 1–5 do not apply in these circumstances.

WHAT ARE THE BASIC PROCEDURES FOR THE VALUER IN PREPARING A RED BOOK VALUATION?

- (1) Decide whether they can/should undertake a valuation by first considering the following questions (PS 1 and PS 2):
 - (a) Is there any actual or potential conflict of interest in carrying out the valuation?
 - (b) Do they have the necessary expertise and experience to carry out the valuation?
 - (c) Are they able to proceed with the instruction without any potential breach of confidentiality?
 - (d) Are there any ethical problems in carrying out the instruction?
- (2) Prepare and agree terms of engagement with client (VPS 1) choosing relevant valuation basis/bases (VPS 4) and, if necessary, during the valuation assignment, updating these terms of engagement to reflect any changes agreed with client;
- (3) Inspect and measure property to extent agreed with client (VPS 2);
- (4) Carry out valuation using any relevant evidence (VPS 5);
- (5) Produce report (VPS 3);
- (6) Ensure process has been properly recorded/documented (VPS 4).

PS 1 and PS 2 in the Red Book address the ethical and professional standards expected of valuers who

‘must at all times act with integrity and avoid any actions or situations that are inconsistent with their professional obligations. They must bring the required levels of independence and objectivity to bear on individual assignments, applying *professional scepticism* and data where it is to be relied on as evidence.’⁹

What is meant by ‘professional scepticism’? This is a new term which the Red Book explains as ‘an attitude that includes a questioning mind, critically assessing evidence relied on in the valuation process and being alert to conditions that may cause information provided to be misleading’.

As it is fundamental to the integrity of the valuation process, the valuer must have:

- Appropriate experience;
- Skill;
- Judgment for the task in question;
- Always act in a professional and ethical manner free from any undue influence, bias or conflict of interest.

PS 2, 3 and 4 follow the 2017 RICS professional statement ‘Conflicts of interest’, setting out the requirements relating to conflicts of interest.

In addition to evidencing proper formal checking procedures, records must be kept of the decisions made in relation to whether to accept, or to continue an instruction for, the obtaining of informed consent and all measures taken to avoid conflicts of interest arising. If there is any conflict, the instruction must either be declined or a written ‘informed consent’ be obtained from all affected parties agreeing that the instruction may proceed. This should only be sought if proceeding despite a conflict of interest is in

the interests of all of those who are or may be affected.

Affected party(ies) can only give informed consent if the person explaining the position to them is entirely transparent, and also if they are sure that they understand what they are doing — including the risks involved and any alternative options available — and are doing it willingly.

Even if all parties are willing to give informed consents, it is for the valuer to decide whether they wish to continue with the assignment.

TERMS OF ENGAGEMENT (VPS 1)

The valuer must fully understand the client’s needs and the reason for the valuation in order to produce a report which is proportionate to the task and professionally adequate.

The precise format of the terms of engagement may vary — for example, some ‘in-house’ valuations may have standing instructions or other internal policies or procedures — but written terms of engagement are required for all valuation work.

As set out in VPS 1, the terms of engagement must address the following matters.

Identification and status of the valuer

A statement is required confirming:

- That the valuation will be the responsibility of a named individual person who is able to provide an objective and unbiased valuation;
- Whether or not the valuer has any material connection or involvement with the subject asset or the other parties to the valuation assignment;
- If there are any other factors that could limit the valuer’s ability to provide an impartial and independent valuation. Such factors must be disclosed confirming that the valuer is competent to undertake the valuation assignment;

- If the valuer needs to obtain material assistance from others in relation to any aspect of the assignment, the nature of such assistance and the extent of reliance must be clear, agreed and recorded.

Identification of the client(s)

It is essential to identify the actual client, as instructions for a valuation may come from someone such as a manager acting for the directors of a company other than the entity to whom the report is to be addressed. If the addressee and the entity responsible for payment of the fee are different, appropriate confirmation of instructions should be obtained from both parties — for example, if a valuation is required for loan purposes and, although commissioned or the fee paid by the borrower or an entity acting for the lender, the report may be for the lender or its subsidiaries. Similarly, a valuation required for estate management or estate-related revenue filings, although commissioned by a financial adviser or an attorney, may be for the estate, the true client.

If the client is a registered company, it may be prudent to quote the actual company registered number; while a company can easily change its name, it cannot change its registered number.

Identification of any other intended users

It is important to understand whether there are any other intended users of the valuation report, their identity, and their needs, in order to ensure that the report content and format meets those users' needs and also to be aware of the risks to the valuer in allowing other intended users.

To meet this requirement, the Red Book suggests that:

- The valuer must state whether or not any parties other than the client may rely upon the valuation;
- In many cases, it will only be the valuer's

client who is seeking reliance upon the valuation. Agreeing to extend reliance to third parties may significantly increase the risks to the valuer;

- As a default position, valuers should confirm that they do not permit third-party reliance on the valuation report in their terms of engagement. Any permitted reliance on the valuation by a third party should be carefully considered and the terms on which reliance is permitted should be documented. Particular care is required to ensure that the valuer does not unwittingly become exposed to the risk of third parties claiming that a duty of care has been extended to them, and that any relevant terms of business (such as limitations on liability) apply to third parties who are permitted to rely on a valuation. Legal advice may be required.

Care should be exercised in considering whether assignment of the valuation engagement contract (as distinct from permitting third parties to rely upon it) is to be permitted, as doing so may expose the valuer to additional risks. Requisite cover in the terms of professional indemnity insurance should be checked where assignment is permitted.

Identification of the asset(s) or liability(ies) being valued

The property or properties to be valued must be clearly identified and agreed with the client, as well as the interest that the client requires to be valued.

When valuing a property interest that is subject to a tenancy, it may be necessary to identify any improvements undertaken by tenants and to clarify whether or not they are to be disregarded on renewal, or review, of the lease, or even if they may give rise to a compensation claim by the tenant when vacating the property. Trade fixtures and fittings, etc. are normally excluded unless valuing an interest in property as part of an operational entity.

Valuation (financial) currency

This is really only likely to be relevant if either the client is based in another country or the properties being valued are in several countries — in which case, the currency to be adopted should be agreed as well as the basis of any exchange rate.

The purpose of the valuation

The purpose of the valuation must be confirmed at the outset of the instruction to establish if it is a valuation that is subject to the Red Book and to confirm the appropriate basis of value. For example, market value might be irrelevant to a client who was seeking a valuation for a purpose requiring a market rent.

It is important that valuations are not used out of context or for purposes for which they are not intended and if the client declines to reveal the purpose of the valuation, it may be difficult to comply with all aspects of the Red Book. In such circumstances, if the valuer is willing to proceed with the valuation, the client must be advised in writing that this omission will be referred to in the report and the report must not be published or disclosed to third parties. If an unusually qualified valuation is to be provided, the terms of engagement should clearly state that it is not to be used for any other purpose than that originally agreed with the client.

The basis, or bases, of value

It is imperative to set out and define the bases to be used. They must be appropriate for purpose. The main bases of value are set out in VPS 4 in the Red Book (global edition) using the IVS definitions from IVS 104 'Bases of value':

- *Market value*: '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 had acted

knowledgeably, prudently and without compulsion';¹⁰

- *Market rent*: 'The estimated amount for which an interest in real property should be leased on the valuation date between a willing lessor and a willing lessee on appropriate lease terms in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion';¹¹
- *Investment value (or worth)*: 'The value of an asset to a particular owner or prospective owner for individual investment or operational objectives';¹²
- *Equitable value*: Formerly known as fair value (IVSC definition), 'the estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties';¹³
- *Synergistic value (or marriage value)*;¹⁴
- *Liquidation value*: 'The amount that would be realised when an asset or group of assets are sold on a piecemeal basis. Liquidation value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity.'¹⁵

Of these IVS defined bases, the most commonly used are market value for capital valuations, which replaced the term 'open market value' some years ago as the approved defined basis.

The definition of market rent used for rental valuations is similar to that for market value. It should be noted, however, that in this case the definition refers to 'appropriate lease terms' and it is essential that these are clearly stated in the valuation. For example, the rent would differ considerably depending upon who was assumed to be responsible for repairs or, even more fundamentally, whether the rent being quoted was an annual, quarterly, or even monthly figure.

Investment value can cause confusion for some clients who assume it to be the market

value of an investment property. Accordingly, it is probably better described as worth, since it represents the worth to a particular client based on their assumptions, which may not accord with that of the market as a whole. It is recommended that the figure should be reported as being solely for the use of the client and their professional advisers, with a caveat that it might not represent market value due to potential differences in assumptions.

Equitable value is what was previously known as the IVSC definition of fair value which has at last been renamed to avoid confusion with the accountancy definitions also described as fair value. It represents the price that would be reasonably agreed between two specific parties for the exchange/sale of an asset. Although the parties may be unconnected and negotiating at arm's length, the asset is not necessarily exposed in the wider market. In addition, the price agreed may be one that reflects the specific advantages (or disadvantages) of ownership to the parties involved rather than the market at large. The valuation may involve an element of synergistic or marriage value since one party may pay in excess of market value to get control of an asset.

It may also arise when valuing a 'ransom strip' where the value to one specific purchaser may be considerably in excess of the value of the land to the market in general.

Finally, liquidation value is used in very specific circumstances to arrive at a net amount likely to be received by the vendor since, unlike market value, it deducts the costs of the sale.

When undertaking valuations for accounts, specific definitions produced by the appropriate accounting body are used. Those defined by the International Accountancy Standards Board (IASB) are:

- *Fair value (IAS IFRS13)*: 'The price that would be received to sell an asset or paid to transfer a liability in an orderly

transaction between market participants at the measurement date.'¹⁶ Used by companies adopting international accountancy standards.

- *Fair value (FRS 102 2.34 (b))*: 'The amount for which an asset could be exchanged, a liability settled, or an equity instrument granted could be exchanged, between knowledgeable, willing parties in an arm's length transaction.'¹⁷ Used by companies adopting the simplified UKGAAP accountancy standard. This definition is UK specific for use by small to medium-sized enterprises able to file simplified accounts; it is only referred to in the UK National Standards and not in the Red Book Global edition.

In both cases, although described as 'fair value' and using different definitions, it is generally accepted that the actual value is identical to the market value of the property being valued.

The IFRS 13 basis and definition is widely adopted internationally but some other accountancy bodies may use different bases and definitions. Since the client's adopted accountancy standard will determine the definition to be adopted and any specific additional requirements (such as additional comments regarding risk and uncertainty), this should always be checked with the client or their professional advisers when accepting valuation instructions.

To ensure that the client is fully aware of what is being provided, it is suggested that the definition of the basis(es) of value being used be stated in the main body of the terms of engagement (and not just in an appendix to the terms).

Valuation date

Defined in IVS as the date on which the opinion of value applies. This may well be different from the date on which the valuation report is to be issued or the date on which investigations are to be undertaken

or completed. The specific valuation date will need to be agreed with the client. An assumption that the valuation date is the date of the report is not acceptable nor should it be a projected future valuation date.

Nature and extent of the valuer's work – including investigation – and any limitations thereon

Any limitations or restrictions on the inspection, inquiry and analysis for the purpose of the valuation assignment must be set out in the terms of engagement.

If relevant information is not available because the conditions of the assignment restrict the investigation, then records of these restrictions and any necessary assumptions or special assumptions should be recorded — for example, a short timescale for reporting or a 'desktop' valuation rendering it impossible to establish facts that would normally be verified by inspection, or by making normal enquiries.

While a client may require or accept this level of service, it is the valuer's duty to discuss the requirements and needs of the client prior to reporting. Any such restriction should be considered as to whether reasonable, regarding the purpose for which the valuation is required.

Consideration may be given to accepting the instruction subject to certain conditions, such as that the valuation is not to be published or disclosed to third parties, but if it is not possible to provide a valuation, even on a restricted basis, the instruction should be declined.

It must be made clear when confirming acceptance of such instructions that the nature of the restrictions and any resulting assumptions, and the impact on the accuracy of the valuation, will be referred to in the report (see also VPS 3, valuation reports).

Nature and source of the information upon which the valuer may rely

This refers to any relevant information

(including data and other such inputs) that is to be relied upon and the extent of any verification to be undertaken during the valuation process must be agreed and recorded.

- Where the client will provide information that is to be relied on, this should be stated clearly in the terms of engagement and, where appropriate, its source and any references or dates on the document. In each case the extent to which the information to be provided is likely to be reliable must be considered;
- Information that is accepted as reliable should be referred to as an assumption;
- If the client expects an opinion on legal issues that affect the valuation, it must be made clear in the report what information needs to be verified by the client's or other interested parties' legal advisers before the valuation can be relied on or published.

Assumptions and special assumptions to be made

All assumptions and any special assumptions that are to be made in the conduct and reporting of the valuation assignment must be recorded.

Assumptions are matters that are reasonable to accept as fact in the context of the valuation assignment without specific investigation or verification. They are matters that, once stated, are to be accepted in understanding the valuation.

A special assumption is an assumption that either assumes facts that differ from the actual facts existing at the valuation date or that would not be made by a typical market participant in a transaction on the valuation date.

Special assumptions are often used to illustrate the effect of changed circumstances on value.

When valuing a development site, the residual appraisal method requires a gross development value. This would be a future

value once the building is completed and sold, however, whereas market value must not be projected beyond the date they are being carried out (see ‘valuation date’ above). To satisfy this requirement, the gross development value will be the current market value and reflect the current market conditions subject to the special assumption that the proposed building had actually been completed and was for sale on the valuation date.

Other examples of special assumptions might include an assumption that:

- A specific contract was in existence on the valuation date even if it had not actually been completed;
- There was a reduced marketing period for selling the property; note this is not the same as a ‘forced sale’ — a term which must not be used;
- A planning application had already received consent.

Special assumptions may only be made if they can be reasonably regarded as realistic, relevant and valid for the particular circumstances of the valuation.¹⁸

VPS 2 suggests, particularly in the case of adverse on-site factors, that any matters assumed not to exist can rarely be disregarded completely and should be brought to the client’s attention before the report is issued. For example, if a defect is noted on inspection but the client wants it disregarded it would be a market value with a special assumption which may well differ from market value without such an assumption.

Further guidance on assumptions and special assumptions can be found in VPS 4, ‘Bases of value’, assumptions and special assumptions.

Format of report

Refers to how the valuation will be communicated to the client. In electronic or paper format? How many copies will be provided?

What is the timescale for producing the report? Are there to be any departures from the mandatory reporting requirements set out in VPS 3? etc.

If the report is to be provided in a paperless format, the report should not be sent in Word format since this can be ‘broken’ to disclose previous edits — and possibly other opinions of value. It is safest to scan a copy of the report, although many firms use a pdf version of the file.

Restrictions on use, distribution or publication of the report

Where it is necessary or desirable to restrict the use of the valuation advice or those relying upon it, this should be recorded. If matters are identified that are likely to cause the valuation to be qualified, this must also be recorded.

- Limitations are only effective if notified to the client in advance;
- Professional indemnity insurance (PII) policies may require the valuer to have particular qualifications, and to include certain limiting clauses in every report and valuation. If so, the relevant words should be repeated, unless the insurers agree to either a modification or a complete waiver. If in doubt, refer to the insurance policy before accepting instructions;
- Some valuations will be for purposes where the exclusion of third-party liability is either forbidden by law or by an external regulator. In other cases, it will be a matter for clarification or agreement with the client, and the valuer’s own judgment.

Confirmation that the valuation will be undertaken in accordance with the IVS

The valuer should provide confirmation that:

- The valuation will be undertaken in accordance with the IVS and the valuer will assess the appropriateness of all significant inputs.

Or (depending on client's particular requirements):

- The valuation will be undertaken in accordance with the 'RICS Valuation – Global Standards', which incorporate the IVS, and (where applicable) the relevant RICS national or jurisdictional supplement. Where appropriate, such confirmation may be abbreviated to refer simply to the Red Book Global.

In both cases an accompanying note and explanation of any departures from the IVS or the Red Book Global must be included. Any such departure must be identified, together with justification for that departure, and would not be justified if it results in a valuation that is misleading.

References to the Red Book without reference to the year of issue will be taken to mean the version of the RICS standards operative at the valuation date, provided that it is on or before the date of the report.

Where other valuation standards — specific to a particular jurisdiction — will be followed, this should be confirmed as part of agreeing the terms of engagement.

The basis on which the fee will be calculated

As the RICS does not publish any scales of fees, this is generally a matter to be settled with the client. It may be a fixed fee or a percentage of value and should confirm whether disbursements are included or are charged separately, as well as that VAT (at the appropriate rate) will be added depending upon the client; many valuers ask for the fee upon instruction.

Where the firm is registered for regulation by RICS, reference to the firm's complaints handling procedure, with a copy available on request

This is a long-standing requirement is to emphasise the need for RICS-regulated firms to comply with the RICS 'Rules of Conduct for Firms', paragraph 7.

A statement that compliance with these standards may be subject to monitoring under RICS's conduct and disciplinary regulations

The purpose of this statement is to draw the client's attention to the possibility that the valuation may be investigated by RICS for compliance.

A statement setting out any limitations on liability that have been agreed

This is a matter to discuss with professional indemnity insurers and the client. RICS will be issuing global guidance, but in the meantime, it suggests referring to the latest guidance applicable in the jurisdiction.¹⁹

The terms as set out in VPS 1 are just the minimum mandatory requirements; the list should be extended to suit the particular instruction. As mentioned previously, VPGA 1 and 2 provide further guidance on additional matters to be included for valuations for accounts and loans respectively.

INSPECTIONS (VPS 2)

Inspections and investigations must always be carried out to the extent necessary to produce a valuation which is professionally adequate for its purpose. Thus, provided it is agreed with the client and they are aware of the limitations, a limited or even a 'desktop' valuation may be quite acceptable in some circumstances.

The scope of the inspection should be covered within the terms of engagement if

restricted in scope as it could also lead to material uncertainty (see 'Valuation report').

All measurements must be taken in accordance with the appropriate IPMS/ Code of Measuring Practice and, even if the client requests measurements on the previous (CMP 6th edition) basis, the IPMS measurements and calculations should also be available on the file for types of property where IPMS is now mandatory.

The valuer should consider the surrounding area as well as the subject property itself since this could affect value, eg whether an improving or deteriorating area, other properties for sale or to let, physical matters that may affect the property such as flooding, access, Japanese knotweed, etc.

Refer to VPGA 8 for further guidance on matters relating to inspections including their scope.

VALUATION REPORT (VPS 3 AND IVS 103)

Irrespective of the client, it is essential that the report should:

- (a) Be clear;
- (b) Not be misleading or create a false impression;
- (c) Be unambiguous;
- (d) Cover all matters agreed with the client in the final terms of engagement;
- (e) Use terms that can be understood by someone who is not a property expert (the 'man on the Clapham omnibus').²⁰

The actual format and detail of the report are matters for the valuer and the client to agree in the terms of engagement. If the client supplies a form of report they require, it should be checked to ensure it covers the substance of the listed minimum terms. If it does not and the omission is material, the matter should be discussed with the client. Any reasons for any divergence from the minimum required terms of engagement

must be recorded in order to comply with the requisite standards.

A minimum of 16 matters must be included in a report.²¹ They are as follows:

- (a) Identification and status of the valuer;
- (b) Identification of the client and any other intended users;
- (c) Purpose of the valuation;
- (d) Identification of the asset(s) or liability(ies) to be valued;
- (e) Basis(es) of value;
- (f) Valuation date;
- (g) Extent of investigation;
- (h) Nature and source(s) of the information relied upon;
- (i) Assumptions and special assumptions;
- (j) Restrictions on use, distribution or publication of the report;
- (k) Confirmation that the valuation has been undertaken in accordance with the IVS;
- (l) Valuation approach and reasoning;
- (m) Amount of the valuation or valuations;
- (n) Date of the valuation report;
- (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;
- (p) A statement setting out any limitations on liability that have been agreed.

Since most of the items (a–i) generally mirror the final terms of engagement, they may to some extent be 'cut and paste' from the finally agreed terms of engagement to ensure continuity.

For item i), all assumptions and any special assumptions, together with any reservations that may be required to arrive at the reported figure, must be explicitly set out in the report in full together with a statement that they have been agreed with the client.²²

For j), the extent of the investigations undertaken, including the limitations on those investigations set out in the terms of engagement, must be disclosed in the report.

The report must record the date and extent of any inspection, including reference to any part of the property to which access was not possible (see VPS 2).

It must be made clear if the valuation has been made without an opportunity to carry out an adequate inspection²³ or equivalent check.

Where the valuation is undertaken on the basis of restricted information, or is a revaluation without an inspection, the report must include full particulars of the restriction (see also VPS 1, 'Nature and extent of work').

When reporting on h) nature and source of information relied upon where the client has provided such information, the valuer has a responsibility to state clearly that the information is covered by, or in, the terms of engagement (see VPS 1) and, where appropriate, to specify its source. In each case the valuer must judge the extent to which the information to be provided is likely to be reliable and whether any further, reasonable steps are required to verify it.

Conversely, if the valuation has been carried out without information that would normally be, or be made, available, this must be made clear in the report.

It must be stated in the report if verification (where practicable) is needed of any information or assumptions on which the valuation is based, or if any information considered material has not been provided.

If such verification is material to the amount of the valuation, it must be made clear that the valuation should not be relied on without that verification.²⁴

If the client expects the valuer to express an opinion, or the valuer wishes to express an opinion, on legal issues that affect the valuation, the valuer must make clear in the report any information that must be verified by the client's or other interested parties' legal advisers before the valuation can be relied on or published.

The report should state any additional information that has been available to, or

established by, the valuer, and is believed to be crucial to the client's ability to understand and benefit from the valuation, with regard to the purpose for which it has been prepared.

For item k), any valuation complying with the latest edition of the Red Book will be IVS compliant. As set out in the terms of engagement, VPS 3 requires the valuer to provide confirmation of compliance.

Additionally, an accompanying note and explanation of any departures from the IVS or the RICS Red Book Global must be included. A departure would not be justified if it resulted in a valuation that is misleading.

With regard to l) valuation approaches, the Red Book states:

'To understand the valuation figure in context, the report must make reference to the approach or approaches adopted, the key inputs used and the principal reasons for the conclusions reached.

This requirement does not apply if it has been specifically agreed and recorded in the scope of work that a valuation report shall be provided without reasons or other supporting information.'²⁵

For the distinction between approach and method see VPS 5, paragraph 1.

Valuation approaches would be 'market approach' (ie comparison method), 'income approach' (ie investment method or possibly profits method) or 'cost approach' (ie depreciated replacement cost method).

The extent of description of these should be proportionate to the task, focused on assisting understanding by the client and other intended users. The supporting reasons, or rationale, for the conclusions reached should, where relevant, include an explanation of any deviation from common practice within the profession.

In practical terms, if more than one method can be used to arrive at a valuation — for example, investment method backed

up by comparable sales — this should give greater confidence in a valuation figure.

When undertaking valuations of development sites, it should be noted that the RICS Guidance Note Global ‘Valuation of development property’ 1st edition October 2019, effective from 1st February, 2020 states that:

‘Best practice avoids reliance on a single approach or method of assessing the value of development property. Normally, any valuation undertaken by the market comparison approach should be cross-checked by reference to the residual method. Where a residual method is used, it is similarly important to cross-check the outcome with comparable market bids and transactions where they exist, including the subject property. The advice to apply both methods when possible has been endorsed by 2019 amendments to IVS 410 (effective from 31 January 2020).’

The Guidance Note also provides guidance on contents of the report.

When setting out in the report item m) the amount of the valuation(s), the figure(s) must be given in figures and in words to avoid any confusion. Although it is not a specific requirement within the Red Book, it is suggested that the name and definition of the basis should be in the same section — eg ‘the market value (which is defined as ...) of the subject property is £x (words).’

To avoid any confusion or misunderstanding by the client, it may be advisable that the basis (including the definition) should be as close as possible to the valuation figure relating to it in the report. For valuations that may be relied upon by parties other than the client who commissioned it or to whom it is addressed, further disclosures set out in PS 2, paragraph 5²⁶ need to be included.

If a part of the property being valued has a negative value, this should be stated separately and not just aggregated as this

could produce a potentially distorted overall figure.²⁷

Item o) merits further explanation.

Valuations are sometimes described as an ‘opinion of value’ since they rely on a valuer’s interpretation of evidence of other transactions and their relevance.

Because of this the courts have accepted that there is likely to be a degree of variation (differences in professional opinion) in the figure. If outside of such accuracy, there is considered to be *material* uncertainty with a mandatory requirement for specific comment by the valuer. In the UK for residential valuations this would normally be expected to be within a range of plus or minus 5 per cent, and for commercial properties plus or minus 10–15 per cent.

VPGA 10 sets out three main categories that might give rise to such uncertainty:

- (1) The characteristics or type of property may make it difficult for the valuer to form an opinion of the likely value, regardless of the approach or method used — for example, valuing properties for which there are numerous comparable sales would allow a greater degree of certainty than for valuing a unique property such as a stately home or even a windmill;
- (2) Valuations with limited or restricted information available either as a result of the client’s instructions or the circumstances of the valuation which cannot be sufficiently addressed by adopting one or more reasonable assumptions. This may apply for ‘desktop valuations’ or when full title documentation is not available;
- (3) Disruption to the markets such as by unforeseen financial, macro-economic, legal, political or even natural events. Typical examples of the latter might be when valuing immediately after the Brexit referendum or following the collapse of Lehman Brothers in 2008 or, most recently, the effects of the

COVID-19 pandemic on the market. In such cases, the market had changed, rendering any evidence from prior to the events potentially irrelevant in the new market conditions.

At the time of writing this paper, the effects of the COVID-19 pandemic are still upsetting the markets — particularly for commercial properties. The RICS has produced guidance for valuers in the form of ‘Valuation Practice Alerts’ which are regularly updated. They include a proposed wording for reports which should be considered before issuing any valuation report.²⁸

As mentioned previously, valuers may be required to comment on uncertainty, irrespective of whether it is material uncertainty, for valuations for accounts in order to comply with the requirements of the accountancy bodies. This should be clarified with the client or their professional advisers prior to accepting instructions.

BEFORE ISSUING THE REPORT

Matters frequently occur during the inspection and information gathering processes that were not originally envisaged, but which will have to be included in the terms of engagement. It is therefore vital that, before issuing the report, all matters have been fully brought to the attention of the client and fully documented. Thus, there may well be further matters included in additional terms of engagement agreed with the client up to issue of the report. Clearly any assumptions or special assumptions must be agreed as these will be included in the report. Under no circumstances should the report be submitted to the client until the terms of engagement have been agreed and documented²⁹ and they must accord with the client’s requirements and what is being undertaken for the client. Many valuers send a further copy of the final terms of engagement as an appendix to the report.

Has the whole process of carrying out this assignment been properly documented on the files? This should be sufficient for a third party to be able to review the whole process, including the reasoning behind the final reported valuation figure.

VALUATION METHODS (VPS 5 AND IVS 105)

Although IVS 105 ‘Valuation Approaches and Methods’ covers valuation methods in some detail, VPS 5 does not specifically prescribe which method to use or how to value and states that ‘valuers are responsible for adopting, and as necessary justifying, the valuation approach(es) and the valuation methods used to fulfil individual valuation assignments’. These must always have regard to:

- The nature of the asset (or liability);
- The purpose, intended use and context of the particular assignment; and
- Any statutory or other mandatory requirements applicable in the jurisdiction concerned.

It states that valuers should ‘also have regard to recognised best practice within the valuation discipline or specialist area in which they practise but that ‘this should not constrain the proper exercise of their judgment in individual valuation assignments in order to arrive at an opinion of value that is professionally adequate for its purpose’.

It emphasises that it is the valuer who is ultimately responsible for selection of the approach(es) and method(s) to be used — unless expressly required by statute or by other mandatory requirements, no one valuation approach or single valuation method.

Finally, it must again be stressed that this paper can only provide a brief outline of the basic Red Book requirements as at November 2020; there will generally be further requirements depending upon such

matters as the type of property, the reason for the valuation and the jurisdiction in which the property is situated. There may also have been updates to reflect changes in statute, case law, practice and market changes.

Any opinions expressed in this article are those of the author and do not necessarily represent those of RICS, IVSC or iSurv. The valuer should check the latest edition of the Red Book,³⁰ the latest relevant National Standards and any other guidance issued by RICS (whose copyrights are acknowledged).

NOTES AND REFERENCES

- (1) 'Red Book', Part 1, 'Introduction', p. 3. See RICS (2017), 'RICS Valuation – Global Standards 2017', available at <https://www.rics.org/globalassets/rics-website/media/upholding-professional-standards/sector-standards/valuation/red-book-2017-global-edition-rics.pdf> (accessed 7th December, 2020).
- (2) RICS (2017), 'RICS Valuation – Global Standards 2017: UK national supplement', available at <https://www.rics.org/globalassets/rics-website/media/upholding-professional-standards/sector-standards/valuation/red-book-uk-supplement-rics.pdf> (accessed 7th December, 2020).
- (3) They are set out in PS 1 5.4.
- (4) Where global practice statement and guidance note applies, see RICS (2016), 'Real estate agency and brokerage guidance', 3rd edn, available at <https://www.rics.org/globalassets/rics-website/media/upholding-professional-standards/sector-standards/real-estate/real-estate-and-agency-brokerage-3rd-edition-rics.pdf> (accessed 7th December, 2020).
- (5) This is because the specific rules and procedures laid down by the court, tribunal or judicial body must be followed. See RICS (2014), 'Surveyors acting as expert witnesses', 4th edn, available at <https://www.rics.org/globalassets/rics-website/media/upholding-professional-standards/sector-standards/dispute-resolution/surveyors-acting-as-expert-witnesses-4th-ed-sep-2020.pdf> (accessed 7th December, 2020).
- (6) Where the relevant statutory provisions will define the task and also, frequently, the manner in which it is to be carried out. The emphasis is on the word 'function' relating to the performance of a statutory role or duty involving the exercise of statutory powers involving the formal appointment of an individual. Thus, the provision of a valuation for inclusion in a statutory return to a tax authority which involves compliance with the law but not the exercise or enforcement of it does not fall within this exception.
- (7) This is now recognised as possibly being when advice is sought by a client — often a regular portfolio valuation client — that will not be released to third parties, eg in connection with proposed asset management initiatives or proposed acquisitions. Such advice often does not attract an additional fee and this element of valuation service may or may not be specifically referred to in the terms of engagement for a regular portfolio revaluation. The terms of engagement or written advice must, however, be quite explicit about the prohibition of disclosure to any other party and/or the use for any other purpose and exclusion of liability.
- (8) It covers valuation advice on probable outcomes of current or impending negotiations or requests figures to be quoted in connection with such negotiations.
- (9) See PS 2 1.5 for this requirement.
- (10) VPS 4.4.
- (11) VPS 4 5.
- (12) VPS 4 6.
- (13) IVS 104, paragraph 50.1.
- (14) RICS, glossary of technical terms.
- (15) IVS 104, paragraph 80.1: 'Liquidation Value can be determined under two different premises of value: (a) an orderly

- transaction with a typical marketing period (see section 160), or (b) a forced transaction with a shortened marketing period (see section 170). A valuer must disclose which premise of value is assumed.'
- (16) The definition adopted by the International Accountancy Standards Board (IASB) in IFRS 13: 'The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.'
 - (17) 'The amount for which an asset could be exchanged, a liability settled, or an equity instrument granted could be exchanged, between knowledgeable, willing parties in an arm's length transaction.' (FRS 102 2.34(b)).
 - (18) VPS 4, paragraph 9.
 - (19) RICS (January 2018), 'Professional Standards and Guidance, UK: Risk, Liability and Insurance in Valuation Work', 2nd edn, available at <https://www.rics.org/globalassets/rics-website/media/upholding-professional-standards/sector-standards/valuation/risk-liability-and-insurance-in-valuation-work-2nd-edition-rics.pdf> (accessed 10th December, 2020).
 - (20) VPS 3 1.
 - (21) Set out in VPS 3, paragraph 2 along with RICS commentary on them.
 - (22) VPS 3, paragraph 2.2(i).
 - (23) VPS 2, paragraphs 1.2 and 1.7.
 - (24) VPS 1 3.2(j).
 - (25) VPS 3 2(l).
 - (26) These relate to valuations of publicly quoted companies, pension funds, etc. and include provisions relating to length of time as a signatory to the report, proportion of fee income etc., see PS 2 5 for further details.
 - (27) VPS 3 2.2 (m) 8.
 - (28) See RICS, 'Valuation practice alert – COVID-19', available at <https://www.rics.org/uk/upholding-professional-standards/sector-standards/valuation/valuation-coronavirus/> (accessed 7th December, 2020).
 - (29) PS 2 7.
 - (30) RICS, 'Red Book Global Standards', <https://www.rics.org/uk/upholding-professional-standards/sector-standards/valuation/red-book/red-book-global/> (accessed 7th December, 2020).