RICS guidance note

RICS Professional Guidance, European Union

EUGN 1: EU directives and regulations relevant to valuation

1st edition

rics.org/standards

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1st edition, November 2013

RICS

Published by the Royal Institution of Chartered Surveyors (RICS)

Parliament Square

London

SW1P 3AD

UK

www.rics.org

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ISBN 978 1 78321 028 2

Typeset in Great Britain by Columns Design XML Ltd, Reading, Berks

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RICS guidance notes

This is a guidance note. Where recommendations are made for specific professional tasks, these are intended to represent 'best practice', i.e. recommendations which in the opinion of RICS meet a high standard of professional competence.

Although members are not required to follow the recommendations contained in the note, they should take into account the following points.

When an allegation of professional negligence is made against a surveyor, a court or tribunal may take account of the contents of any relevant guidance notes published by RICS in deciding whether or not the member had acted with reasonable competence.

In the opinion of RICS, a member conforming to the practices recommended in this note should have at least a partial defence to an allegation of negligence if they have followed those practices. However, members have the responsibility of deciding when it is inappropriate to follow the guidance.

It is for each member to decide on the appropriate procedure to follow in any professional task. However, where members do not comply with the practice recommended in this note, they should do so only for a good reason. In the event of a legal dispute, a court or tribunal may require them to explain why they decided not to adopt the recommended practice. Also, if members have not followed this guidance, and their actions are questioned in an RICS disciplinary case, they will be asked to explain the actions they did take and this may be taken into account by the Panel.

In addition, guidance notes are relevant to professional competence in that each member should be up to date and should have knowledge of guidance notes within a reasonable time of their coming into effect.

This guidance note is believed to reflect case law and legislation applicable at its date of publication. It is the member's responsibility to establish if any changes in case law or legislation after the publication date have an impact on the guidance or information in this document.

Document status defined

RICS produces a range of professional guidance and standards products. These have been defined in the table below. This document is a guidance note.

Type of document	Definition	Status
Standard		
International Standard	An international high level principle based standard developed in collaboration with other relevant bodies	Mandatory
Practice Statement		
RICS Practice Statement	Document that provides members with mandatory requirements under Rule 4 of the Rules of Conduct for members	Mandatory
Guidance		
RICS Code of Practice	Document approved by RICS, and endorsed by another professional body/stakeholder that provides users with recommendations for accepted good practice as followed by conscientious practitioners	Mandatory or recommended good practice (will be confirmed in the document itself)
RICS Guidance Note (GN)	Document that provides users with recommendations for accepted good practice as followed by competent and conscientious practitioners	Recommended good practice
RICS Information Paper (IP)	Practice based information that provides users with the latest information and/or research	Information and/or explanatory commentary

EUGN 1: EU directives and regulations relevant to valuation

Introduction

1 This guidance note draws valuers' attention to the need for particular care when undertaking valuation work on which various EU directives and regulations may impact. It is essential that the work is undertaken in the light of knowledge of the existence of the directives or regulations, as the case may be, and with an understanding of how they are to be implemented in individual Member States. Care must also be taken to ensure that valuation reports draw attention to any aspects of the directives or regulations – or, more particularly, their implementation – of which the client needs to be aware in order to understand and use the report for its intended purpose.

2 Valuers providing valuations for specific purposes within the EU will normally refer to the regulatory requirements that apply in the relevant country. Those local rules must reflect the framework set out by the directives or regulations. Although it may not be necessary to refer to them directly, valuers should be aware of their relevance and impact. National association valuation standards (see PS 1 paragraph 5, RICS national association valuation standards), where they have been provided, will set out the relevant local regulatory requirements.

- An 'EU directive' is a legislative act which member states are required to transpose into national legislation. A directive normally states the desired outcome, but leaves member states with a certain amount of leeway as to the exact rules to be adopted. When adopted, directives give member states a timetable for the implementation of the intended outcome.
- An 'EU regulation' is directly enforceable in the member states and therefore does not need to be transposed.

3 The directives and regulations in Table 1 are those that either:

- provided the original framework for regulation of the financial statements of specified entities or
- harmonised some of the prudential rules for financial institutions and operators.

Table 2 lists some of the amending directives where they affect the valuation requirements. The list of directives in Table 2 is not comprehensive.

Table 3 contains brief details of miscellaneous directives and regulations that have an impact on the valuation process.

4 The text of the directives may be obtained from the following web address: http://eur-lex.europa.eu/RECH_menu.do?ihmlang=en. This link is to the search page of the

English version of the directives, but links are also provided to all other language translations throughout the EU. These legislative texts are also available from the RICS EU Liaison Team at +32 (0)2 739 42 28 or euaffairs@rics.org

Table 1: Principal EU legislation applying to valuation

Regulation (EU) 575/2013 and **Directive 2013/36/EU**	**EU capital requirements directive (CRD IV)** Introduces Basel III provisions into EU legislation and repeals CRD directives 2006/48/EC and 2006/49/EC, dividing them into: (a) a *directive* governing access to deposit-taking activities and (b) a *regulation* establishing the prudential requirements institutions and firms need to respect. Matters with important links to national administration laws (i.e. supervision, sanctions, and corporate governance provisions) will remain in the directive, while the detailed and rigid provisions on calculating capital requirements will fall under the regulation. • Incorporates the IVS definition of 'market value' • Defines 'mortgage lending value' as the value of immovable property as determined by an assessment of the future marketability of the property taking into account long-term sustainable aspects of the property, the normal and local market conditions, and the current use and alternative appropriate uses of the property • 'Speculative immovable property financing' is defined as loans for the purposes of acquisition or development or construction of land in relation to such property, with the intention of reselling for profit; the directive places its risk weight to exposures at 150% • Sets out monitoring requirements and defines a valuer as a person who 'possesses the necessary qualifications, ability and experience and who is independent from the credit decisions process' • 'Marking to market' is defined as the valuation of positions at readily available close out prices that are sourced independently, including exchange prices, screen prices, or quotes from several independent reputable brokers • 'Marking to model' signifies any valuation that has to be benchmarked, extrapolated or otherwise calculated from one or more market input • Sets out the frequency of real estate valuations as once a year for commercial, minimum once every three years for residential, and either once every three years or in case of a suspected decline in value for loans exceeding 3 million Euros or 5% of the entity's own funds.
Directive 2013/…/EU (Title subject to change with finalised legislation)	**On credit agreements relating to residential property** This directive intends to create a single market for mortgage credit with a high level of consumer protection, and promote financial stability by enhancing responsible mortgage lending. • Introduces an early repayment option for borrowers • Mandates a creditworthiness assessment of the consumer by the lender; a negative assessment should prevent lenders from granting the loan • Introduces requirements for the advertising of mortgage credit • Member states to ensure that general information about credit agreements is made available by creditors or credit intermediaries. This includes whether or not a property valuation is necessary and, if so, by whom it should be carried out (Article 9(j))

	• Member states to ensure that reliable property valuation standards for mortgage lending purposes are developed within their territory. Member states shall require creditors to ensure that those standards are used where they carry out a property valuation or to take reasonable steps to ensure that those standards are applied where a valuation is conducted by a third party. Where national authorities are responsible for regulating independent appraisers who carry out property valuations they shall ensure that they comply with the national rules that are in place (Article 14(1)) • Member states to ensure that internal and external appraisers conducting property valuations have the professional competence and sufficient independence from the credit process to provide an impartial and objective valuation, a record of which shall be kept by the creditor (Article 14(2)) • Recital 14d specifies that for valuation standards to be considered reliable, they should take into account internationally recognised valuation standards such as IVS and the RICS Valuation – Professional Standards (Red Book).
Directive 2011/61/EU Supplemented by Commission Delegated Regulation 231/2013/EU	**On Alternative Investment Fund Managers** Established common requirements governing the authorisation and supervision of Alternative Investment Fund Managers (AIFMs) in order to reduce excessive financial risk-taking. The valuation procedures used shall ensure that the assets are valued at least once a year. The AIFM shall disclose to investors a description of the valuation procedure and of the pricing methodology for valuing assets before investing in the AIF. The AIFM must ensure that the valuation is performed by either: (a) an external valuer completely independent from the AIF, AIFM and any other person with close ties to them or (b) the AIFM itself if the valuation task is functionally independent from the portfolio management and remuneration policy, and if no conflicts of interest or undue influence on the employee(s) exists. Where an external valuer is used: • The AIF must show that the valuer is subject to mandatory professional registration recognised by law, legal or regulatory provisions or rules of professional conduct • The AIF must show that the valuer can provide sufficient professional guarantees demonstrating the ability to effectively perform the relevant valuation function • The valuer may not delegate the valuation task to a third party. The Regulation introduces level 2 measures that further harmonise the implementation of AIFM Directive across the EU. Where valuation is concerned: • Improperly carried out valuations of assets or calculations of unit/share prices shall be considered a professional liability risk • As part of the general requirements, the AIFMs must establish, implement and maintain valuation rules and accounting policies permitting them to provide a financial report at the request of the competent authorities • The AIFM shall not invest in a certain type of asset for the first time unless an appropriate valuation methodology has been identified for that specific type of asset • The valuation policies shall establish the obligations, roles and responsibilities of all parties involved in the valuation process, and shall address certain conditions including, but not limited to, controls over the selection of valuation inputs, escalation channels for resolving differences in valuing assets, and the appropriate time for closing the books for valuation purposes (section 7, Articles 67 to 74).

Directive 2011/ 61/EU continued	Comment: The implementation of this Directive, and the valuer's role and liability under it, is a complex area. Valuers undertaking work to which it applies must not rely on this as a summary, but instead make appropriate enquiries and – where necessary – take advice to ensure they fully understand their role and responsibilities, including their exposure to potential liability.
Directive 78/ 660/EC	**Fourth Council Directive on the annual accounts of certain types of companies** Sets out the basic requirements for recognition of assets in company accounts of public companies (excluding banks, other financial institutions and insurance companies). Originally provided that valuations should be based on the principle of purchase price or production cost. National law variations to be disclosed (section 7, articles 31 to 42). Method applied (cost/revaluation/replacement) to be noted in accounts.
Directive 83/ 349/EEC	**Seventh Council Directive on consolidated accounts** Originally, under article 29, valuations were to be provided in accordance with Directive 78/660/EEC.
Directive 86/ 635/EEC	**On the annual accounts and consolidated accounts of banks and other financial institutions** Effectively applies 78/660/EC to asset valuations of banks and financial institutions (section 7, articles 35 to 39).
Directive 91/ 674/EEC	**On the annual accounts and consolidated accounts of insurance undertakings** Effectively applies 78/660/EEC to asset valuations of insurance companies but allows current value to be on the basis of market value on the valuation date. Revaluations to be at not more than five-year intervals (section 7, Articles 45 to 62). 'Market value' is defined in the directive as: '… the price at which land and buildings could be sold under private contract between a willing seller and an arm's length buyer on the valuation date, it being assumed that the property is publicly exposed to the market, that market conditions permit orderly disposal and that a normal period, having regard to the nature of the property, is available for the negotiation of the sale.' Although this definition differs in detail, it is considered that a valuation at market value as defined in VPS 4 paragraph 1.3, Market value, will give the same result.

Table 2: Amendments of directives in Table 1

Directive 90/604/ EEC	**Amending Directives 78/660/EEC as concerns the exemptions for small and medium-sized companies and the publication of accounts in ecus Method applied (cost/revaluation/replacement) to be noted in accounts** Increasing certain monetary thresholds to simplify administrative procedures for small and medium-sized enterprises.
Directive 90/605/ EEC	**Amending Directives 78/660/EEC and 83/349/EEC with regard to the scope of those directives** Extension of company types to comply with these directives.
Commission Recommendation 2000/408/EC	**Concerning disclosure of information on financial instruments and other items complementing the disclosure required according to Council Directive 86/635/EEC** Banks and financial institutions are to disclose information according to the annex.
Directive 2001/ 65/EC	**Amending Directives 78/660/EEC, 83/349/EEC and 86/635/EEC with regard to the valuation rules for the annual and consolidated accounts of certain types of companies, as well as of banks and other financial institutions** Allows all valuations under the amended directives to be at fair value.
Regulation (EC) 643/2005	**Repealing Regulation 2909/2000 on the accounting management of the non-financial fixed assets** Effective as of 1 January 2005, 'accounting rules and methods shall be adopted by the Commission's accounting officer' in agreement with article 133(1) of financial Regulation 1605/2002.
Regulation (EC) 1004/2008	**Amending Regulation (EC) 1725/2003 adopting certain international accounting standards in accordance with Regulation (EC) 1606/2002** Adopts amendments to IAS and IFRS allowing the reclassification of certain financial instruments.
Directive 2003/ 51/EC	**Amending Directives 78/660/EEC, 83/349/EEC, 86/635/EEC and 91/ 674/EEC on the annual and consolidated accounts of certain types of companies, banks and other financial institutions and insurance undertakings** Removes inconsistencies between the above four directives and IAS, and amends them. Allows fair value as a basis of value.
Directive 2009/ 49/EC	**Amending directives 78/660/EEC and 83/49/EEC as regards certain disclosure agreements for medium-sized companies and the obligation to draw up consolidated accounts** Exempts medium-sized companies from the disclosure requirement on formation expenses. Exempts parent undertakings from the obligation to provide consolidated annual accounts and a consolidated annual report if it only has immaterial subsidiaries.

Table 3: Miscellaneous directives and regulations

Directive 2006/ 123	**On services in the internal market** Provides that: • member states shall respect the right of providers to provide services, which include valuation services, in a member state other than that in which they are established and • the member state in which the service is provided shall ensure free access to, and free exercise of, a service activity within its territory. Sets out rules on the limited extent to which the provision of services may be restricted.
Commission Communication 97/C 209/03	**Commission Communication on State Aid Elements in sales of land and buildings by public authorities** Gives guidance on the procedure to handle sales of publicly owned land in a way that automatically precludes the existence of state aid. In broad terms, a sale by auction is recommended but if that is not the route taken an independent valuation has to be provided to establish the market value of the land. The definition of market value is as set out in Directive 91/674/EEC (see Table 1).
Commission Communication 2009/C 72/01	**Commission Communication on the treatment of impaired assets in the Community banking sector** Focuses on the issues to be addressed by member states in considering, designing and implementing asset relief measures. 'Impaired assets' correspond to categories of assets on which banks are likely to incur losses. While assets should first be valued at current market value, 'real economic value' will be used for impaired assets as the current market value may be quite distant from the book value of those assets, or in some cases nonexistent in the absence of a market. 'Real economic value' is defined as 'the underlying cash flow of a given asset over time'. The assessment of the real economic value should be based on observable market inputs and realistic and prudent assumptions about future cash flows (Annex IV Section 1). As the value attributed to impaired assets is in the context of an asset relief program, real economic value will be higher than the market value in order to achieve the relief effect. Valuations of different pre-defined categories of assets need to be certified by an independent third party expert and validated by the national supervisory authority. The valuation must be based on internationally recognised standards and benchmarks.

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RICS has a worldwide network. For further information simply contact the relevant RICS office or our Contact Centre.

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