Investment Property Forum

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Response by the Investment Property Forum (IPF) to the RICS public consultation on proposed changes to UK regulated purpose valuation practice

The IPF welcomes the opportunity to engage in the public consultation on the RICS Red Book UK Supplement revisions to UK VPS 3.3 covering rotation. We outline below our thoughts on the proposals for:

- A time-limited, mandatory rotation cycle for regulated purpose valuations; and
- The policy intended to provide clients with a reasonable timescale to transition.

About the IPF

The IPF is a UK-wide membership organisation of senior professionals, all active in the property investment and finance market. The IPF has a diverse membership of 1,800, which includes valuers, fund managers, investment agents, accountants, bankers, lawyers, researchers, academics, actuaries and other related professionals.

The IPF's Mission is to enhance the understanding and efficiency of property as an investment, including public, private, debt, equity and derivatives, for its members and other interested parties, including government. The IPF's scope covers direct and indirect routes to investing in property. With regards to the latter, we have an Indirect Property Interest Group that covers issues relating to both the listed and unlisted property sector, including that of the illiquidity of property as an asset class.

IPF comments on the proposals

- **A time-limited, mandatory rotation cycle for regulated purpose valuations.**

The RICS's proposed changes to UK VPS 3.3 envisage that, from 1 October 2023, the valuer and firm rotation arrangements will see a mandatory maximum five-year continual contractual relationship period for valuation services for a Regulated Purpose, with the option of up to a three-year extension period, subject to a successful service review. This is followed by a mandatory break of five consecutive years until the next permitted instruction of that valuer and/or firm.

Our response to these changes is primarily in respect of real estate funds that are valued on a frequent basis (monthly/quarterly). Our comments are based on soundings taken from the Managers of these funds by the Association of Real Estate Funds (AREF) and the IPF.

We have seen various comments that infer the proposed arrangements in UK VPS 3.3 mirror the rules on auditor rotation. This is not the case. The rules for rotation of an audit firm were set out in section 491 of the Companies Act, but now are in section 494ZA. This section provides that, in the case of Public Interest Entities, the audit is required to go out to tender after 10 years and there is mandatory rotation of the audit firm after 20 years, see: https://www.legislation.gov.uk/ukpga/2006/46/section/494ZA. The requirement for rotation at five years is for the audit partner, not the firm, and is in the Financial Reporting Council (FRC) ethical

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guidance, see: https://www.frc.org.uk/getattachment/601c8b09-2c0a-4a6c-8080-30f63e50b4a2/Revised-Ethical-Standards-2019-Updated-With-Covers.pdf.

We think that it would be more appropriate for UK VPS 3.3 to reflect the existing rules on auditor rotation as set out above, rather than adopting the timescales proposed by the RICS. This is based on the following reasons:

a. Consistency between the rotation rules for auditors and valuers.
b. Reduction in the disruption of the set-up period for valuers undertaking frequent (often monthly) valuations of portfolios.
c. Reduction in the friction costs associated with the changeover of valuation firms for both clients and valuers.
d. Provision of a longer period of certainty for valuers to build and maintain the large valuation teams required to undertake frequent valuations, particularly if valuers are required to undertake detailed DCF valuations and analyse comparable evidence using the same methodology.

Regulated purpose valuations include valuations for all types of collective investment schemes and unregulated property unit trusts. We believe a mandatory five-year rotation would be particularly problematic for many closed-ended funds that have a seven-to ten-year fixed life, with the possibility of a one- or two-year extension to complete the disposal of assets. It would be usual to conduct tenders at the outset and to appoint valuers to provide typically annual valuations for the duration of the fund. Auditors are also typically appointed for the duration of the fund. Having a mandatory rotation as the fund disposes of its investments in the wind-down phase is unlikely to be popular with investors.

If the auditor rotation timescales are adopted, the valuer would be in place for the duration of the fund. If a fund's duration was extended for any length of time, the valuation appointment would be subject to tender, but the same firm could be reappointed following this as the mandatory rotation of the valuer firm is after 20 years.

- **The policy intended to provide clients with a reasonable timescale to transition**

The use of the existing rules on auditor rotation would minimise client confusion as to contractual relationship periods and provide sufficient flexibility to transition between valuers in the same way that they do between auditors.

Please contact me should you wish to discuss or clarify any of the points raised above.

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