TEGoVA – Setting European Valuation Standards for 40 Years
TEGoVA
THE EUROPEAN GROUP OF VALUERS' ASSOCIATIONS

April 2017 / Issue No. 7

European Valuer

Belgrade welcomes TEGoVA delegates

The 2017 valuation conference season kicks off with a European Valuation Conference in Belgrade on 21st April, followed by TEGoVA's Spring Assembly the next day. The Conference, entitled **"The Influence of the European Union on the Development of a Modern Valuation Profession in Serbia"**, will feature eminent speakers, including **Zlatko Milikic**, Assistant to the Minister of Finance, Serbia, **Michael MacBrien**, adviser to TEGoVA and director general of the European Property Federation, **Sandra Rodic**, Expert, USAID Serbia Business Enabling Project, **Scott Robinson**, Immediate Past President, Appraisal Institute, Professor **Richard Grover**, Oxford Brookes University, **Roger Messenger** Vice Chairman of TEGoVA and **Krzysztof Grzesik**, TEGoVA Chairman.

The Conference and Assembly coincides with the implementation of a recently enacted statute on valuer licensing in Serbia. The new law, which seeks to ensure financial stability and to address systemic risk in the banking system, was passed with the developmental support of a special working group established by the Ministry of Finance, with help from USAID, under the Business Enabling Project in Serbia. The National Association of Valuers of Serbia (NAVS) was also closely involved in the project. A valuers' licence may be issued to a candidate who holds a recognised university degree or post-graduate diploma and successfully completes professional training and a test, the latter from an accredited organisation. A candidate must also undertake at least three years of work experience in property valuation and finally pass a state licensing examination.

However, the statute does recognise the professional designations of TEGoVA, The

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TEGoVA breaches the final frontier – valuation methodology

This year marks the 40th anniversary of TEGoVA (originally 'TEGoVoFA'). For four decades, TEGoVA has been the voice of Europe's valuation profession and its valuation standard setting body, publishing and regularly updating its flagship product, the **'Blue Book'** of European Valuation Standards. Leading valuers from across Europe have contributed to the Blue Book's amazing body of knowledge and guidance, in the interests of raising the profile of the valuation profession and improving transparency in the real estate market.

But the realisation today is that **'standards'** are not enough. It does not follow that because valuers follow European Valuation Standards or other internationally recognised standards, full transparency has been reached in real estate markets across the world if they analyse market transactions in different ways and if they all apply their own versions of the accepted methodologies (comparative, income and cost). For example, in the valuation of commercial property, whilst discounted cash flow (DCF) methodology is now widely applied, it is not done consistently. There is no consensus about whether cash flows should be growth **'implicit'** or **'explicit'**, or about the nature of the appropriate discount rate to be applied, or indeed the meaning of the multiplicity of market yields used for valuation purposes. For the last 40 years, the focus has been on valuation standards rather than methodology, the latter becoming largely the preserve of academics. For decades, practitioners have stayed clear of seeking ways of harmonising valuation practice. Such a situation is no longer tenable at a time when clients are questioning the diversity of methodologies applied even within the same jurisdiction. Indeed many clients wrongly perceive valuation standards to be about methodology. They are not. Thus TEGoVA makes no apology for boldly going where standard setters have failed to go before. The aim is not to encroach on academic endeavour but to formulate a **'collective'** practitioners' view on methodological issues and to draft user friendly guidelines. Words such as **'must comply'** will be missing from such guidelines. At the same time, TEGoVA will seek closer cooperation with top real estate academics and this journal will seek learned contributions from them. Professor Nick French's excellent article in this edition is a case in point.

At TEGoVA's Assembly in Dublin last October, a new European Valuation Practice and Methodology Board (EVPMB) was established under the Chairmanship of **Philippe Guillerm** FRICS REV (AFREXIM). The Assembly endorsed the other EVPMB members as follows: **Dana Ababei** MAA MRICS REV (ANEVAR), **Adriano Callé Lucas** FRICS REV (ASAVAL), **Estanislao de Kostka de la Quadra-Salcedo Capdevilla** MRICS (AEV), **Leandro S. Escobar Torres** MRICS REV (ATASA), **Georg Flödl** MRICS (ÖVI), **Danijela Ilić** FRICS REV (NAVS), **Dr Theodor Konstantakopoulos** MRICS (AVAG), **Nick Millard** FAAV MRICS REV (CAAV) and **Stephan Zerbe** CIS HypZert (F/M) MRICS REV (VÖB). In the first instance, the EVPMB will review, update and develop further, TEGoVA positions on valuation methodology. It will also respond to methodological issues as they arise, in particular the assessment of Mortgage Lending Value and the accuracy of Automated Valuation Models. The EVPMB will facilitate Europe-wide discussion on methodological issues. Currently the EVPMB is reviewing the Income Approach, putting more focus on the difference between implicit and explicit DCFs, distinguishing between investment valuation and market valuation, differentiating between implicit and explicit cash flows and differentiating between **'equated'** yield and

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Royal Institution of Chartered Surveyors (RICS) and The Appraisal Institute (AI). During a transitional period of up to 18 months, all valuers in Serbia holding a REV, RICS Registered Valuer or MAI designation will be **"grandfathered"** into the new cadre of licensed valuers without the need to fulfill any additional requirements. In this respect, NAVS is proud to have ensured that its REV-designated members are afforded a smooth stress-free transition to the elite community of Serbian (and other European!) valuers.

NAVS feels very proud and privileged to host the upcoming TEGoVA spring meetings and offers a warm welcome to its friends from 65 valuers' associations, representing 35 countries from Europe and beyond. ●

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To contribute to this journal, contact the Editor, John Roberts, on jcroberts54@hotmail.com

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'equivalent' yield. The EVPMB will also take a more detailed look at the Comparative Approach, including the selection of comparables and process of comparison.

The above said, TEGoVA will not lose sight of the continuous process of updating European Valuation Standards. A newly constituted European Valuation Standards Board (EVSB) under the Chairmanship of **Dr Michael Reinberg** FRICS CRE REV (ARE) has also recently met for the first time. A report on its work will follow in the next edition of *European Valuer.* ●

Krzysztof Grzesik REV, Chairman TEGoVA.

Professor Nick French presents the art of real estate valuation

Valuation is not a science! It may utilise quantitative techniques to assess value but it is actually a heuristic process of identifying and quantifying market price in the absence of an actual sale or letting. Thus when we consider the value of a property in terms of rent or capital value, we are actually looking at the question, *"how much will occupiers and investors be willing to pay for the subject building?"*

Valuation is primarily concerned with comparison. The general tenet is that a purchaser/occupier will pay a similar price to buy/rent space as other players in the market. Thus the valuer uses this relationship to determine price/rent by comparing recent sales/lettings of similar properties in the market. These **'comparables'** are the principal ammunition in the armoury of the valuer. The better the comparable, in terms of specification, timing, location and legal interest, the better the price of one property will relate to another. Ideally, the valuer will rely upon a set of comparables and, using his/her knowledge of the market, determine an appropriate value from the information available.

Whilst TEGoVA's latest European Valuation Standards (EVS 2016) do not suggest which valuation model one should adopt, **Information Paper 5** (EVIP 5) does discuss the approaches and methods available to a valuer and provides clear and helpful details of the process that should be followed when carrying out a valuation. **EVS 2016 is a quality assurance document. It should be seen as the starting point and treated as the valuer's bible.**

If the basis of valuation is market value, the valuer will be attempting to estimate the price at which the subject property would sell for on the day of the valuation. The difficult question is how does the valuer achieve this? This is where the art and the science and the process come together. To determine the price of the subject property, the valuer needs to assess what the market has recently been paying for similar properties in the area. These comparables provide **signposts** to the likely price of the subject property. As they are neither definitive nor infallible, they have to be interpreted. That is the art of the valuation – determining the appropriate inputs for the valuation model, which is the science of the valuation. Together, they form the process.

Price, value and worth

To understand this viewpoint fully, it is important to understand the distinction between **'price', 'value' and 'worth'**. These are similes in normal usage but in valuation, and indeed in terms of economic definitions, they are distinct and separate concepts. Price is the observable point of exchange whereas the EVS definitions for value and worth are as follows;

Market value is, *"The estimated amount for which the property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without being under compulsion."*

Worth (or Investment Value) is, *'The value of a property to a particular identified party for investment, owner-occupation or operational purposes'.*

This can be illustrated by a very simple analysis by reference to the market bids (by tender) for a property. Assume that **'the property'** is placed on the market and that there are 52 players in the market. Each player assesses the 'worth' of that property to himself or herself, some of them believe the asset to be exactly what they require and are willing to bid a high figure. Others don't want the property at all and will either bid zero or put in a low bid. If we look at their bids, then the following pattern occurs (see Table 1 below). A number of players bid low figures, most bid €10 but one person bids €20. Each of the bids represents that individual's **'calculation of worth'**, but the open market sale occurs not where the majority of the bids are concentrated but at the highest point, which is the bid of the person who has the most bullish view of the property market. He or she is willing to pay €20 because they believe that the property is worth that amount to them. The fact that other players don't share that view will not affect the sale price on that day. Their views however may influence our thinking on the valuation of the property at a later date.

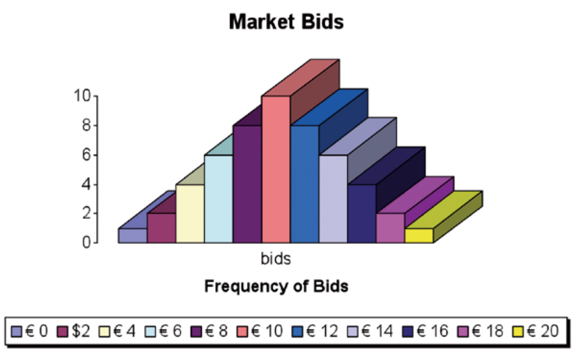
	€0	€2	€4	€6	€8
Number of bids	1	2	4	6	8

€10	€12	€14	€16	€18	€20
10	8	6	4	2	1

Table 1 – market pricing: number of bids

In Table 1, it can be seen that 1 person did not **'like'** the property at all and bid €0. Most people assessed its worth at €10 and the highest frequency of bids happened at that point. However, the price is determined at the highest figure of €20. Graphically, the market has performed as a normal or bell distribution and the sale is determined at the further point on the x-axis. See Figure 1 below.

Figure 1 – market pricing



The person who has bid €20 obviously has the most optimistic view of the performance of that property in the future. Only with hindsight will we be able to determine if his/her view of the world is correct or not. A valuation should therefore attempt to reflect how the buyers in that market would assess the worth of the property and identify what is likely to be the highest and best bid. It is that bid that will determine the market value of that property, not the consensus view. The task of valuers is therefore very difficult – they are attempting to identify not only the best bidder in the market today, but the level of their bid. This cannot be an exact science and as a result, until the sale actually occurs, it must be remembered that the valuation is a 'best estimate' of what that price might be when the sale is completed. **In determining market price, the model adopted should mirror the thought process of the investors/players in the market.**

The above example illustrates that properties trade, all other things being equal, at the highest bid at that moment in time. However, valuers are not privy to that information until after the sale and thus they must look at previous sales (comparables) to gauge the tone of the market. Understanding the mechanics of the local economy is imperative to allow valuers to interpret the information available and estimate price as best as they can. Values will increase from observable prices in a rising market and will fall in a depressed market. Valuers will anchor on the last set of comparables but will adjust their valuation according to their observation of current market sentiment. ●

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UK: A hard exit for property? Brexit has implications for real estate. Perhaps the UK should look at Canada's relationship with the EU for inspiration, writes Michael MacBrien

Many of the freedoms and privileges of EU membership are not recognised as such by real estate professionals but simply taken for granted in an **'open'** and **'global'** economy. Exit from the EU means the end of many of the most basic real estate investment and service provision freedoms, or at least putting them at the mercy of individual countries. It is possible for the EU and the UK to negotiate a treaty that could partially offset this.

The EU internal market is founded on four freedoms – free movement of capital, services, goods and persons. All four are crucial to property. The first guarantees the freedom to buy and sell real estate without obstacle anywhere in the EU. The second enables property professionals of all types to practice anywhere in the EU, with or without establishment and with their home country qualifications. The third enables free circulation of construction products and the fourth creates an open construction labour market framed by EU workers' rights. **Exit from the EU ends all of this.**

Free movement of capital in its broadest and common acceptance will doubtless remain unchanged, but obstacles to real estate investment can be expected to mushroom. For property purchase, it suffices to see how the Australians or Chinese control foreign property investment or how countless other countries let the investor in, but not out. Left to their own devices, Europeans should be no different.

The history of the EU is a long sequence of attempts to raise barriers to property investment – the will to control foreign purchase of land and buildings being a core nationalist reflex. Each attempt was stopped by the **European Commission** – sometimes at the behest of the **European Property Federation** (EPF) – or quashed by the Court of Justice of the European Union (CJEU).

There was one exception. The Danish held up the **Maastricht Treaty** until a protocol was added enabling Denmark to permanently control non-Danish purchase of secondary residences. But that was truly exceptional leverage in a union which otherwise is one big real estate emporium for EU citizens and businesses, while non-EU investors can be subjected to restrictions that are perfectly arbitrary or whose proforma justifications cannot be countered without the Commission or the CJEU.

The most important obstacle to property investment may well be indirect, as part of a panoply of measures restricting service provision. Indeed, direct restrictions on access to real estate are often a part of the classic cocktail of obstructions such as requiring local qualifications, or a licence to operate, or requiring a joint venture with a local party, or restrictions on the legal form of the service enterprise, or putting a percentage cap on foreign presence in an economic sector, or economic necessity tests – all things that took decades of EU law and case law to overcome.

Public procurement will be another sea change. Under EU law, national and local administrations must have pan-European tendering procedures for projects that often are of direct interest to contractors, developers, architects, engineers and town planning consultants. Continental administrations will no longer be obliged to consider offers from UK-based companies, and conversely the British government will be able to reserve contracts for UK nationals as it once unsuccessfully tried to achieve for the now defunct **English Partnerships brownfield redevelopment schemes**.

Tariff-free commerce in construction products and real estate fixtures stops at the EU border, but WTO rules on such products may be enough to obviate this. The greater problem is non-tariff barriers. Today, these are often no longer erected with the specific purpose of protecting markets under bogus health, safety or environmental norms; national rules create obstacles by just being different. In other words, countries with comparable levels of consumer and environmental protection create barriers just by legislating in different ways. The EU obviates this via harmonisation of core law and mutual recognition of the rest, coupled with home country control of the manufacturer. This ends upon exiting the union. The construction business and its clients will need to factor in higher costs for the building blocks of the real estate economy.

The end of the free movement of people could be a positive for the UK property industry. It will be possible to hire European workers with no EU-enforced benefits and no right for the workers to stay in the country and seek other employment.

A partial, Canadian solution

UK membership of the European Economic Area (EEA) would preserve all four freedoms, but at a cost: acceptance of all the freedoms, movement of persons included; payment of a budgetary contribution almost equivalent to the cost of EU membership without many of its funding paybacks; transposition of new EU law into UK law without any power or vote over its making. All of this would play out under the control of a European Court devoid of British judges. The internal market is not static – all further advances will be imposed on the EEA.

The Comprehensive Economic and Trade Agreement (CETA) between Canada and the EU is germane. It is a highly sophisticated **'second-generation'** treaty that makes Canada the country with the closest relationship with the EU. Its modest provisions on free movement of people would be acceptable to the UK and many of its provisions are relevant to real estate.

It is not a template for EU-UK relations, as it is not a **'kit'**. It's a detailed and complex treaty tailor-made for Canada and the EU, and it reflects nine years of hard negotiations, final skirmishes included. But it should be relatively easy to adapt this to the UK, a country currently totally in sync with the internal market.

The freedom to invest in immovable property is specifically covered by CETA. The provision specifically excludes limitations on the total value of transactions or assets. It cannot be compared to ironclad EU protection, and investment funds operating out of Canada have **no EU 'passport'**. But it is a major guarantor.

In the CETA negotiations, Canada converted the EU to 'negative' service lists, meaning that all services not specifically excluded are covered by the treaty's provisions. No service related to real estate is excluded. CETA only guarantees national treatment, whereas EU law enables service providers to operate in the host country on the basis of any home-country rules that have not been **EU-harmonised**. Under CETA, a party is still free to require a licence, membership in a professional organisation or a local agent, but this is still much better than nothing.

CETA empowers Canadian and European professional bodies to organise mutual recognition of qualifications, enabling all parties to practice freely on both sides of the Atlantic.

In an example relevant to real estate, TEGoVA and its member **the Appraisal Institute of Canada** have already recognised their valuation standards and qualifications, an achievement that they can adapt to CETA. TEGoVA and its UK members could conduct a similar exercise that would largely preserve the freedom to provide valuation services between the EU and the UK.

For the free movement of goods, Canadian construction products can have the EU's CE conformity mark accorded to them by EU-recognised local Canadian certifying bodies working to EU specifications and vice versa. A similar agreement between the EU and the UK could preserve the free-flow of construction products.

Under CETA, free movement of persons is restricted to company personnel needed to complete a project or provide after-sales service. The UK should find that acceptable, especially as it may prove crucial to a UK construction or development company needing to send personnel to complete a project.

One of the ground-breaking achievements of CETA for both goods and services is a sophisticated procedure of **'regulatory cooperation'**, enabling the European Commission, the Canadian government and their respective economic and social interested parties to work on their regulation upstream, at the earliest phases of policy formulation, to avoid useless and unintended obstacles to trade. Transferred to EU-UK, this would be a promising way of ensuring minimum friction to real estate business down the line.

British property interests of all types will need to coalesce around **'access'**. They will need to capitalise on their membership of European real estate construction, investment and service federations to keep British and EU real estate as porous as possible. ●

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This article was originally published in the January/February issue of IPE Real Estate.

Join us in Ottawa – Canada's national capital – for the 2017 International Valuation Conference: Valuation Beyond Borders!

Hosted by the Appraisal Institute of Canada and the Appraisal Institute (US), this event is a rare opportunity to network with appraisal professionals across Canada, United States and international markets in breathtaking venues across the city! Enjoy five streams of education with valuation topics that are relevant to valuation professionals across the globe, whether it be residential, non-residential or non-fee practice areas!

Kicking off the conference with the **'Beyond Borders'** theme, the opening ceremony will begin with distinguished speaker, **Dr. Joe MacInnis** – physician, scientist and deep-sea explorer. Dr. Joe MacInnis studies leadership in high-risk environments. In this session, he will talk about the team genius needed to pilot a research sub three miles under the North Atlantic, work on a Special Forces operational team and conduct a spacewalk on the International Space Station.

Following the keynote speaker, valuation experts from several top valuation firms in North America will discuss **"Valuation Across Borders"**, sharing their insights on North American market forecasts as well as valuation challenges, opportunities and trends.

During the event you will have access to various sessions on technology, global reporting standards, European valuation issues, REIT and CMBS markets, international valuation work and much more.

If you arrive early, you won't want to miss the **"behind-the-scene"**, unique valuation tour of key infrastructure projects that have advanced the City of Ottawa's illustrious landscape. Led by real estate valuation expert, Robin Souchen, BA, AACI, P.App of the City of Ottawa's Corporate Real Estate Office, this two-hour walking tour will provide an intimate look into the valuation issues and challenges that his team faced during several downtown development projects. Hear about the valuation solutions that were devised to implement some of the largest infrastructure projects in Canada – from light rail transit to world-class conference facilities, to the protection of heritage properties that makes Ottawa the capital city it is today. Don't miss this once in a lifetime chance to explore Ottawa as a tourist with your **"valuation hat"** on!

In addition to these interesting sessions, there will also be a number of networking opportunities throughout the conference, including a golf tournament on one of Ottawa's premier courses, a welcome reception that provides a breathtaking view of Ottawa's landmarks and, a networking night – **"Countries and Cocktails"** – that will be held at the world-renowned Canadian War Museum.

Valuation Beyond Borders is certain to be one of the top valuation conferences of the year – see you in Ottawa! ●