INSTITUTE OF SINGAPORE CHARTERED ACCOUNTANTS

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ISCA Financial Reporting Guidance 1 (“FRG 1”)

Real Property Valuation for Financial Reporting – Best practices when engaging valuers: Considerations for Scope Of Work (“SOW”) and Valuation Report (“VR”)

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About ISCA's Financial Reporting Committee

ISCA's Financial Reporting Committee ("FRC") is chaired by Mr Reinhard Klemmer and comprises representatives from legal and accounting firms, corporate, regulators and academia in the financial reporting eco-system. FRC's terms of reference include monitoring policy and implementation issues relating to the development of accounting standards internationally and in Singapore, and to identify, understand and address accounting issues faced by professional accountants in Singapore, and provide support through the issuance of guidance.

The terms of reference are executed through FRC with the support of two Sub-Committees, namely the Core Sub-Committee and the Valuation Sub-Committee. The FRC Core Sub-Committee is the technical accounting arm of FRC and comprises various technical accounting subject matter experts from accounting firms. The Core Sub-Committee engages in technical deliberations on emerging accounting issues in Singapore and new or revised accounting developments proposed by the international accounting standards setter.

Preface

Real estate assets such as land and buildings (or in valuation terms, real property interests) are, more often than not, significant assets of companies. These assets are commonly required by accounting standards to be reported at their fair values on the companies' financial statements. It is therefore pertinent for the valuation process of such assets to be efficient and effective for the financial reporting eco-system to function well.

Generally, valuation for financial reporting purposes will involve the valuer ("Valuer") as the professional service provider, the reporting entity as the client ("Client") and the auditor ("Auditor") as the reviewer for audit purposes.

Hence, it will be beneficial for all involved parties to have a clear understanding of the valuation process and the requirements of the relevant accounting standards. For example, one best practice is for the Client to share and discuss the proposed scope of work or terms of engagement for the valuation with the Auditor before appointing the Valuer. Please see Appendix A for the recommended workflow of the engagement process amongst the Valuer, the Client and the Auditor.

ISCA[1], through its Financial Reporting Committee ("FRC"), FRC Valuation Sub-Committee and Property Valuation Working Group, is issuing this Financial Reporting Guidance ("FRG") to facilitate the valuation process amongst the Valuer, the Client and the Auditor for real property valuation that is intended to be used for financial reporting under Singapore Financial Reporting Standards (International) ("SFRS(I)s"), International Financial Reporting Standards ("IFRSs") or Financial Reporting Standards issued by the Accounting Standards Council ("FRSs"). Although this FRG is written with the Singapore context in mind, the best practices shared in the FRG would also apply to valuation of properties outside Singapore for financial reporting under the above-mentioned financial reporting standards.

If you have any queries on this FRG, please contact Lim Ju May, Deputy Director, or Felicia Tay, Manager, from ISCA's Technical Division via email at: technical@isca.org.sg

[1] ISCA gratefully acknowledge and thank the following individuals for their contributions towards the development of this publication:
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Introduction

SFRS(I) 13 *Fair Value Measurement*[2] is applicable to most assets and liabilities that are required to be measured at fair value by other SFRS(I)s. Fair value is a market-based measurement, not an entity-specific measurement. The objective of a Fair Value Measurement ("FVM") is to estimate the price at which an orderly transaction to sell the asset or to transfer the liability would take place between the entity that holds the asset or the liability and market participants. This refers to a transaction that would take place at the measurement date under current market conditions (i.e. an exit price for the entity at the measurement date).

Correspondingly, the International Valuation Standards ("IVS") issued by the International Valuation Standards Council ("IVSC") is a set of widely recognised international valuation standards for the undertaking of valuation assignments, using generally recognised concepts and principles that promote transparency and consistency in valuation practice. Both International Valuation Standards (IVS) 2017[3] and IVS 2020[4] contain a Framework, five general standards and six Asset Standards (including Asset Standard IVS 400 *Real Property Interests* and Asset Standard IVS 410 *Development Property*). A real property interest is defined in Asset Standard IVS 400 as "a right of ownership, control, use or occupation of land and buildings". Simply put, real property interest includes real estate, land and anything permanently affixed to it, and the bundle of legal rights related to the real estate.

Making reference to IVS' relevant requirements, this FRG highlights key considerations relevant to SFRS(I) 13 when determining the scope of work for valuation of real property interest for the preparation of financial statements in accordance with SFRS(I)s, IFRSs or FRSs. In addition, it deals with the relevant requirements in SFRS(I) 13 about valuation information to be disclosed in the financial statements to meet the Client's financial reporting responsibility when preparing financial statements.

[2] SFRS(I) 13 is identical to IFRS 13 *Fair Value Measurement* and FRS 113 *Fair Value Measurement.*
[3] IVS 2017 is effective 1 July 2017
[4] IVS 2020 is effective 31 January 2020

The following table provides a list of commonly used abbreviations in this FRG.

	Abbreviation	**Description**
1	FRG	Financial Reporting Guidance
2	FRSs	Financial Reporting Standards issued by the Accounting Standards Council
3	FVM	Fair Value Measurement in accordance with SFRS(I) 13
4	IFRSs	International Financial Reporting Standards
5	IVS 2017 and IVS 2020	International Valuation Standards issued by the International Valuation Standards Council
6	RFP	Request for Proposal
7	SFRS(I)s	Singapore Financial Reporting Standards (International)
8	SOW	Scope of Work agreed between the Valuer and the Client
9	SSAs	Singapore Standards on Auditing
10	VR	Valuation Report prepared by the Valuer in compliance with SFRS(I) 13

Contents

Considerations for Scope Of Work (“SOW”) and Valuation Report (“VR”)

1 Credential of the Valuer

1.1 The SOW and VR shall include a statement that the Valuer is in a position to provide an objective and unbiased valuation; and has the requisite knowledge and experience to undertake the valuation consistent with the objective of a FVM in accordance with SFRS(I) 13.

1.2 Where applicable, the SOW and VR shall include a statement that the Valuer has relied on other expert(s) to ensure that the valuation undertaken is consistent with the objective of FVM in accordance with SFRS(I) 13. For example, if the valuation work requires the valuation of plant and machinery, another Valuer may be involved in the valuation of plant and machinery.

1.3 The SOW shall include a statement that the Valuer will provide his/her curriculum vitae (“CV”) and registered licence number (if applicable) upon request by the Client.

1.4 The VR shall be signed off by the Valuer in his/her name. When the VR is signed off in the Valuer firm’s name, the VR shall also include the name of the Valuer.

2 Valuer as the Management’s Expert

2.1 The Singapore Standards on Auditing (SSAs) define “Management’s expert” and “Auditor’s expert” as follows:

Management’s expert – “An individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements.” [Paragraph 5(d) of SSA 500 *Audit Evidence*]

Auditor’s expert – “An individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence. An auditor’s expert may be either an auditor’s internal expert (who is a partner or staff, including temporary staff, of the auditor’s firm or a network firm), or an auditor’s external expert.” [Paragraph 6(a) of SSA 620 *Using the Work of an Auditor’s Expert*]

2.2 In this FRG, the Valuer assumes the role of Management’s expert because the Valuer is engaged by the Client to perform the valuation of real property interests for the purpose of the Client’s financial reporting. This is different from assuming the role of Auditor’s expert. A Valuer who assumes the role of Management’s expert prepares the Valuation Report whereas a Valuer who assumes the role of Auditor’s expert reviews the Valuation Report as part of assisting the Auditor to obtain sufficient appropriate audit evidence.

3 Identify the Client and any other intended users

3.1 The SOW shall specify that the Valuer's role also includes responding to the questions on the valuation raised by the Client and the Auditor for the purposes of preparing and auditing the financial statements.

3.2 The SOW shall specify that where feasible, the Valuer would discuss with the Client and the Auditor key valuation matters before commencement of valuation procedures; and before finalisation of the valuation report. The practical identification of key valuation matters that need to be discussed is subject to the professional judgement of the relevant parties and includes but is not limited to the Valuer and Auditor. Examples of key valuation matters, where appropriate, may include items such as basis of value, the valuation date, the valuation subject(s) based on the unit of account[5], selection of valuation currency, significant assumptions, limitations, special assumptions[6] and qualifications, highest and best use of real property interest and valuation approaches.

4 Asset(s) being valued

4.1 It is recommended that the Client, in consultation with the Auditor, issues clear requirements on matters affecting the valuation of the asset for the Valuer to agree upon. Depending on how the real property interest is held or classified, the financial reporting objective and purpose would differ (e.g. investment property fair value accounting or disclosure, purchase price allocations involving real estate or development properties held for sale, impairment testing, lease classification). These may, for example, affect the unit of account of the real property interest; determine the relevant valuation subject(s); and the required granularity of the valuation (e.g. requirement to determine valuations of both land and buildings individually).

4.2 The SOW and VR shall state the valuation subject based on the unit of account of the real property interest and its valuation premise i.e. whether it is valued on the assumptions that it would be used on stand-alone basis, or in combination with other assets.

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[5] Unit of account is defined in SFRS(I) 13 as the level at which an asset or a liability is aggregated or disaggregated in a SFRS(I) for recognition purposes. For example, the unit of account could be the plant and machinery that is housed in a building, or a building on a plot of land.

[6] Where assumed facts differ from the existing facts, it is a special assumption, often used for illustrative purposes. See IVS 104 *Bases of Value*, paragraph 200.4.

5 Purpose of the Valuation

5.1 The SOW and VR shall make reference to the fact that the valuation is for the purpose of, inter-alia, the Client's financial reporting under SFRS(I)s, IFRSs or FRSs; and, if feasible, state the specific accounting purpose (e.g. re-measurement of investment property at fair value, revaluation of property, plant and equipment, testing of property impairment) that requires the valuation of real property interest to be performed in accordance with SFRS(I) 13.

5.2 It is a requirement of IVS 104 *Bases of Value* that regardless of instructions and inputs provided to the Valuer, the Valuer should not use a basis of value that is inappropriate for the intended purpose of the valuation. The appropriate basis of value for financial reporting purposes is fair value as defined in SFRS(I) 13. Given this stated purpose of valuation, a valuation report using any other bases of value may not be in compliance with IVS 2017 and may not be useful for the Client's financial reporting purposes.

6 Basis of value for financial reporting

6.1 The SOW and VR shall state the basis of value.

6.2 The appropriate basis of value for financial reporting purposes is fair value as defined in SFRS(I) 13. SFRS(I) 13 sets out in a single SFRS(I) a framework for measuring fair value.

6.3 Under SFRS(I) 13, fair value is defined as "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".

6.4 SFRS(I) 13 applies to all financial reporting standards that require or permit fair value measurements or disclosures about fair value measurements in specified circumstances. When engaging a Valuer to report on the valuation of real property interests for financial reporting purposes, the Client should instruct the Valuer to conduct and report on the valuation on the basis of fair value as defined in SFRS(I) 13 in order to comply with the applicable financial reporting standards. The Client is advised to engage a Valuer who would be able to conclude its valuation of the real property interests under fair value as defined in SFRS(I) 13.

7 Valuation date

7.1 Fair value measurement date (e.g. balance sheet date, transaction date, date of impairment assessment) varies according to the financial reporting purpose of the valuation. For practical reasons, the valuation date (e.g. at end of month) may be close to but not at the FVM date specified by the relevant accounting purpose. It is recommended that the Valuer shall confirm and agree with the Client in consultation with the Auditor, the appropriate valuation date after considering the required FVM date and the pertinent circumstances. The SOW and VR shall clearly state the valuation date agreed with the client.

8 Nature and extent of the Valuer's work and any limitations thereon; Nature and source of the information upon which the Valuer relies

8.1 The SOW shall require (and the VR shall disclose) the extent of investigation and nature and source of information to be relied upon by the Valuer that would allow the Valuer to perform a valuation that meets the objective of FVM in accordance with SFRS(I) 13. Specifically, the Valuer is expected to:

a. take into account the characteristics of the real property interest being valued that market participants would consider when pricing the real property interest at the valuation date. Examples of such characteristics may include the nature of the real property interest (i.e. superior or subordinate interest or right to use), the specification, condition and location of the property, in-place tenancy or lease contracts, environmental risks affecting the property, the relevant legal framework that affects the property including but not limited to permissions or restrictions, if any, on the sale or use of the property as well as any expected or potential changes thereto;

b. exclude from the real property valuation, items that are not characteristics of the real property interest being valued (e.g. transaction costs[7]);

c. determine the principal market (or, in the absence of a principal market, the most advantageous market) on which the valuation assumptions are based, including the exit market for an orderly transaction; market participants and the related assumptions; market conditions existing at the valuation date, and the relevant observable inputs;

d. determine the characteristics of market participants (consistent with SFRS(I) 13 definition) on whom the valuation and pricing assumptions are based;

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[7] SFRS(I) 13 paragraph 25 requires that the price in the principal (or most advantageous) market used to measure the fair value of the asset shall not be adjusted for transaction costs. Transaction costs shall be accounted for in accordance with other SFRS(I)s. Transaction costs are not a characteristic of an asset or a liability; rather, they are specific to a transaction and will differ depending on how an entity enters into a transaction for the asset or liability.

Transaction costs, as defined in SFRS(I) 13 Appendix A, are costs to sell an asset or transfer a liability in the principal (or most advantageous) market for the asset or liability that are directly attributable to the disposal of the asset or the transfer of the liability and meet both of the following criteria:

(a) They result directly from and are essential to that transaction.
(b) They would not have been incurred by the entity had the decision to sell the asset or transfer the liability not been made.

e. consider the highest and best use of the real property interest being valued, which may differ from its current use. Highest and best use is the use that would maximise the real property interest's value and that is physically possible, legally permissible and financially feasible. Highest and best use might provide maximum value through its use in combination with other assets as a group, or on a stand-alone basis. An entity's current use of a non-financial asset is presumed[8] to be its highest and best use unless market or other factors suggest that a different use by market participants would maximise the value of the asset.

f. apply valuation techniques (market, replacement cost and/or income approach) that are appropriate in the circumstances and for which sufficient data are available to perform the valuation, maximising the use of relevant observable inputs, and minimising the use of unobservable inputs;

g. determine the point within a range of values indicated by a range of valuation inputs and/or use of multiple valuation techniques that is most representative of the fair value of the real property interest in the circumstances under current market conditions; and

h. provide a conclusion on the fair value (as defined in SFRS(I) 13) of the real property interest being valued.

8.2 The SOW and VR shall state any restrictions imposed and any necessary assumptions made with respect to the above points to enable the Client and the Auditor to assess whether the FVM objective of SFRS(I) 13 has been met.

9 Significant assumptions and special assumptions

9.1 The SOW shall require the Valuer to disclose sufficient details in the VR of all significant assumptions and special assumptions made. A significant assumption is one that can have a significant impact on value, or one where a reasonable variation in the assumption could materially affect the measurement of the accounting estimate. A special assumption is one where the assumed facts differ from the existing facts, often to illustrate the effect of a change in the current circumstance (for example, assuming a proposed building had been completed or a tenanted property had been available for vacant possession).

10 Restrictions on use, distribution or publication

10.1 The SOW shall specify the extent of consent/approval for any reference to the valuation that can be made in the financial statements where the VR(s) is (are) featured.

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[8] As stated in SFRS(I) 13 paragraph 29

11 Confirmation that the valuation will be undertaken in accordance with recognised professional valuation standards

11.1 Although the FVM and disclosure objectives of SFRS(I) 13 are not affected by the valuation standards adopted, it is desirable for the valuation to be performed under recognised professional valuation standards (such as IVS 2017, IVS 2020 and SISV Valuation Standards and Practice Guidelines) for greater uniformity.

12 Information required in the Valuation Report

12.1 The SOW shall require inclusion in the VR, sufficient information to allow the Client and Auditor to:

a. make their own assessment of whether the objective of FVM in accordance with SFRS(I) 13 has been met based on the information that provides evidence that the key measurement provisions of SFRS(I) 13 have been appropriately addressed. Areas that may warrant more detailed descriptions include:
   - valuation methodologies adopted and underlying reasons;
   - key characteristics of real property interest affecting assumptions made;
   - key assumptions for valuation of property under development;
   - highest and best use that differs from the Client's current use, including assessment of physical possibility, legal permissibility, and financial feasibility;
   - basis and results of selecting inputs such as comparable properties, discount rates and capitalisation rates;
   - rationale and basis for making adjustments to observable inputs;
   - basis used to conclude on fair value where a range of values exist or multiple techniques are used, and the rationale and weightage placed;
   - nature, extent and reasons for inclusion of buyer's and or seller's transaction-related costs;
   - use of highly specialised entity-developed model or for which there are no observable inputs; and
   - instances of conflict between observable and/or unobservable inputs.

b. understand the significant assumptions made (i.e. inputs used that are significant to the valuation); major sources of estimation uncertainty in the valuation; and whether assumptions made reflect market conditions.

c. understand the fair value hierarchy[9] (i.e. Levels 1, 2 or 3) of the significant valuation inputs used in the valuation. The hierarchy is dependent on whether the inputs are observable or unobservable.

d. provide information that meets the disclosure objectives and requirements of SFRS(I) 13. Such information would depend on the Client's disclosure requirements that are mainly driven by:
   - whether the valuation is categorised as Level 2[10] or Level 3[11] under the fair value hierarchy;
   - whether the valuation is used for fair value accounting or for disclosure only; and
   - where fair value accounting is applied, whether it is recurring (e.g. remeasurement of investment property at fair value at each reporting date) or non-recurring (e.g. for impairment testing).

12.2 The following are examples of disclosures required to be made by the Client in the financial statements:

a. For all Level 2 and Level 3 valuations:
   - Description of valuation technique(s) and inputs used;
   - Any changes in valuation technique(s) used and reason(s) for change; and
   - Whether the highest and best use of property differs from the Client's current use and the reason for any difference.

b. For all Level 3 valuations (except those performed for disclosures only):
   - Quantitative information about significant unobservable valuation inputs

c. For Level 3 valuations used for recurring fair value accounting:
   - A narrative description of the sensitivity of the valuation to changes in unobservable inputs[12] (including description and likely effect of any interrelationships between inputs) if a change in those inputs to a different amount might result in a significantly higher or lower valuation.

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[9] SFRS(I) 13 paragraph 72 states that "To increase consistency and comparability in fair value measurements and related disclosures, this SFRS(I) establishes a fair value hierarchy that categorises into three levels (see paragraphs 76–90) the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1 inputs) and the lowest priority to unobservable inputs (Level 3 inputs)."

[10] SFRS(I) 13 paragraph 81 defines Level 2 inputs as "inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly".

[11] SFRS(I) 13 paragraph 86 defines Level 3 inputs as "unobservable inputs for the asset or liability".

[12] This includes any adjustments made to the valuation inputs and or the overall computation to in arriving at the fair value.

Appendix A

Recommended workflow of the engagement process of valuation amongst the Client, the Valuer and the Auditor

STEP	PROCESS	INVOLVEMENT OF		
		CLIENT	VALUER	AUDITOR
	Preparation for engagement of Valuer			
1	Identification of the need for valuation: • Consider the intended use(s) of VR that may include financial reporting (and the relevant financial reporting standards), fulfilment of loan covenants etc. • Determine the date of valuation required if the VR is to be used for more than one purpose. • Consider any relevant characteristics of the real property interest that may affect the valuation	YES	N/A	YES
2	Request for Proposal ("RFP"): • Ensure that the intended use(s) or purposes of valuation and date of valuation are stated clearly in the RFP.	YES	N/A	N/A
3	Discussion of the scope of work and information required in VR which may include the following: • Intended use(s) of valuation report and valuation date; • Key valuation matters, including basis of value, unit of account etc.; • Relevant characteristics of the real property interest; and • Need for specific disclosures or information for the intended user(s) of the VR.	YES	YES	YES
	During the valuation & before finalisation of valuation			
4	Discussion of any issues that the Valuer encountered in the process of valuation, if needed.	YES	YES	IF NEEDED
5	Discussion on key valuation matters, including changes, if any, from the scope of work agreed before commencement of work.	YES	YES	YES
	After finalisation of draft VR			
6	Respond to Auditor's inquiries on valuation matters	YES	YES	YES