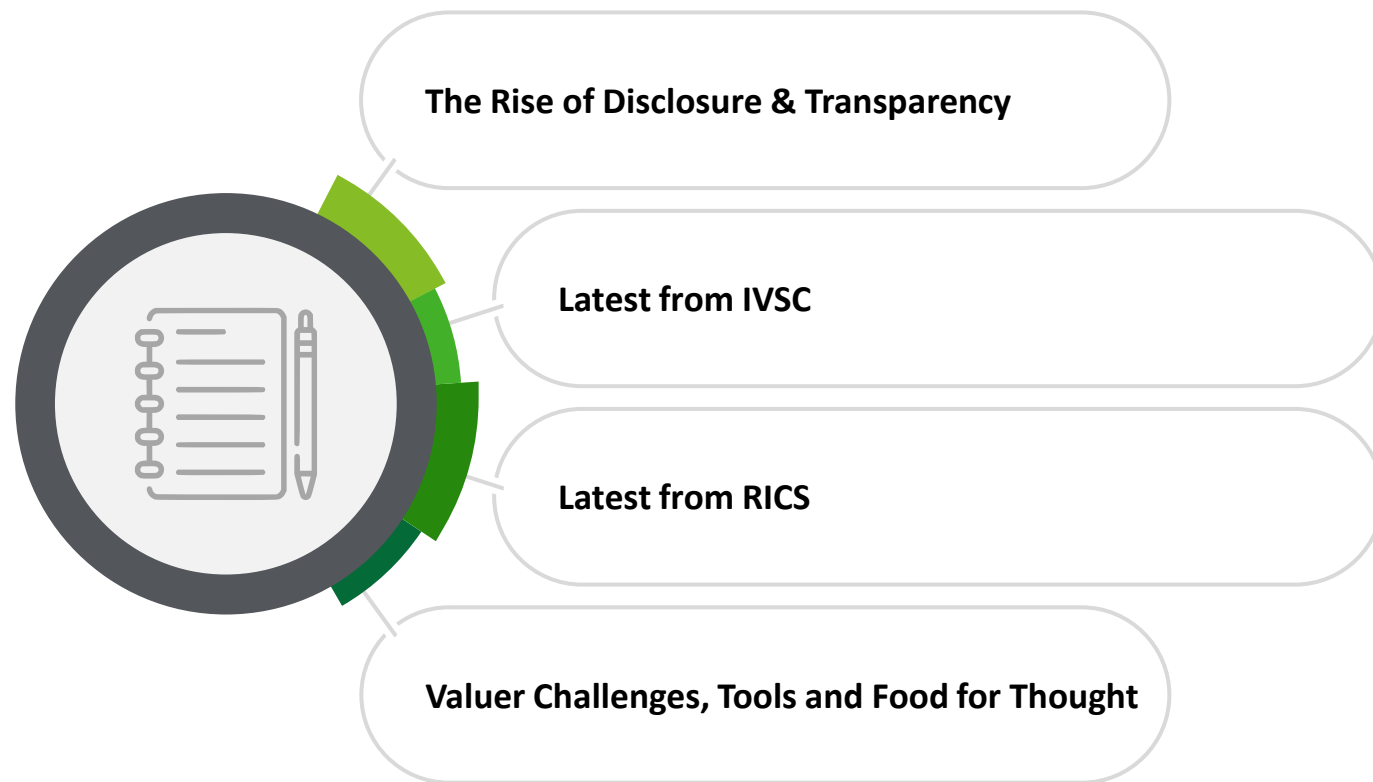


ESG & Valuation Status Update The tide of greater transparency

Philip Parnell, Partner, Valuation & ESG
Autumn 2022

Spotlight increasingly on Valuers and Valuation

Agenda



Investors and businesses must have the information they need to understand the full range of environmental risks they face and create. That information should be a key component of every investment decision and the strategy of every business. Climate and environmental considerations should be central to the decision-making process of every UK board and every investor's risk and return calculations.

- Rt Hon Rishi Sunak MP, (former) Chancellor of the Exchequer



Taskforce on Climate Related Disclosures (“TCFD”)

Rapid adoption and a key driver for the evolution of Regulatory and Reporting Standards



Annual Status Report

User Feedback:

- Over nine out of ten consultation respondents identified as users find disclosure of financial impacts useful.
- Rating agencies stated that climate-related information is an increasingly important input into their financial impact assessments, informing the rating process
- Will be improved with more disclosure on:
 - The amount of expenditure or capital investment currently deployed toward climate-related risks and opportunities
 - The amount of expenditure or capital investment to be deployed to meet targets for addressing climate risks and opportunities, often disclosed in transition plans;
 - Interconnected reporting linking qualitative disclosures with their actual and potential financial impact.

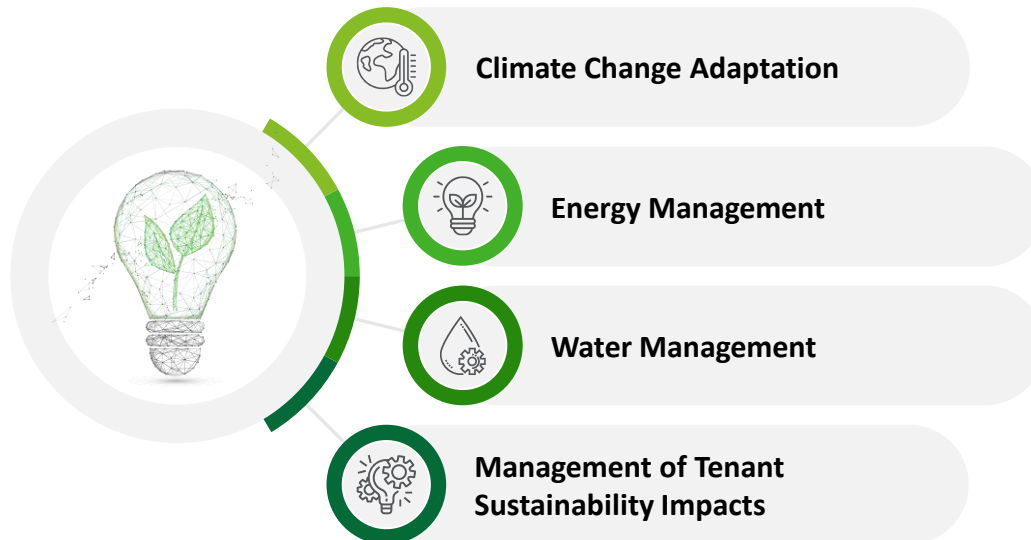


IFRS – Evolving to align with TCFD requirements

Intended to “form a comprehensive global baseline of sustainability disclosures designed to meet the information needs of investors in assessing enterprise value.”

International Sustainability Standards Board

- Formed at COP26
- Drafts of IFRS S1 and S2 issued in March 2022:
 - **S1 – General Sustainability-Related Disclosures**
 - **S2 – Climate-related Disclosures**
(Real Estate specific content within Volume B36)
- Consultation closed at end-July 2022 – new standards targeted by year-end
- Will require a blend of “Quantitative” and “Discussion & Analysis” reporting/disclosure



IVSC – Recognition....but more to come?

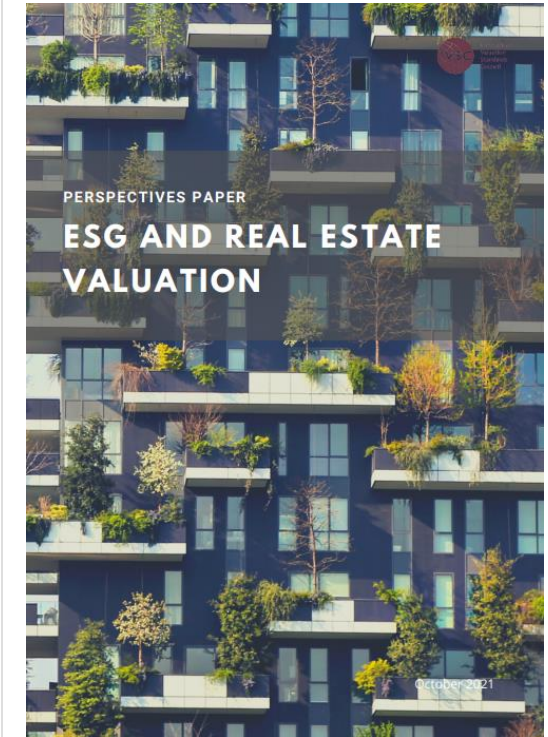
Yet to explicitly recognise ESG within it's Standards, yet cognisant of the issues.

ESG deemed to be “implicit” within the requirements of the International Valuation Standards

- IVS 101 20.1 “all valuation advice and the work undertaken in its preparation must be appropriate for the intended purpose.”
- IVS 102 20.1 “investigations made during the course of a valuation assignment must be appropriate for the purpose of the valuation assignment and the basis(es) of value”.

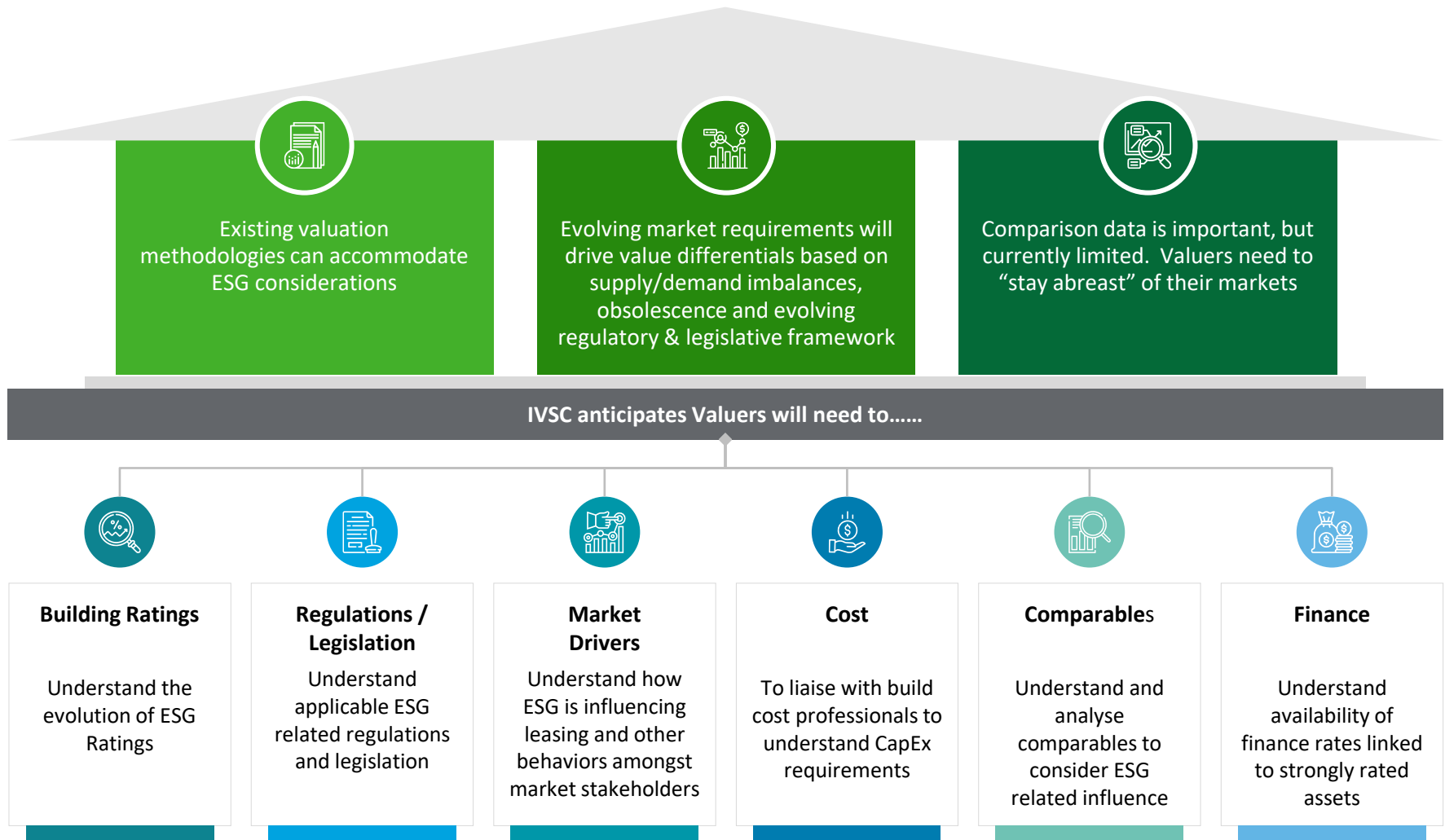
The Paper also connects the ability to link ESG factors explicitly within cash flow projections and references for Development Property appraisals

- IVS 105 50.36 - 50.4, the adjustments for additional risks within the cash flow projection require detailed consideration and this will include ESG elements.
- IVS 410 Development Property section 100 provides the following requirements in relation to the Asset:
 - “(c) whether there are other nonfinancial obligations that need to be considered (political or social criteria),
 - (k) sustainability and any client requirements in relation to green buildings,”



IVSC – Expectations moving forwards

IVSC's Perspectives Paper identifies key valuation drivers – the consideration of which will require valuers to continue to build knowledge.



The RICS Red Book – Valuation process and reporting is evolving

Subtle but important updates were made in the January update with a strengthening of language and more explicit reference across the breadth of ESG.

VPS 2 Inspections, investigations and records

“...‘sustainability and ESG matters’. Such factors are commonly important in terms of market and societal perception and influence, and valuers should have proper regard to their relevance and significance in relation to individual valuation assignments.”

VPS 3: Valuation Approach & Reasoning

“...wherever appropriate, the relevance and significance of sustainability and ESG matters should form an integral part of the valuation approach and reasoning supporting the reported figure.”

VPGA 8: Valuation of real property interests Sustainability – assessing the implications for value

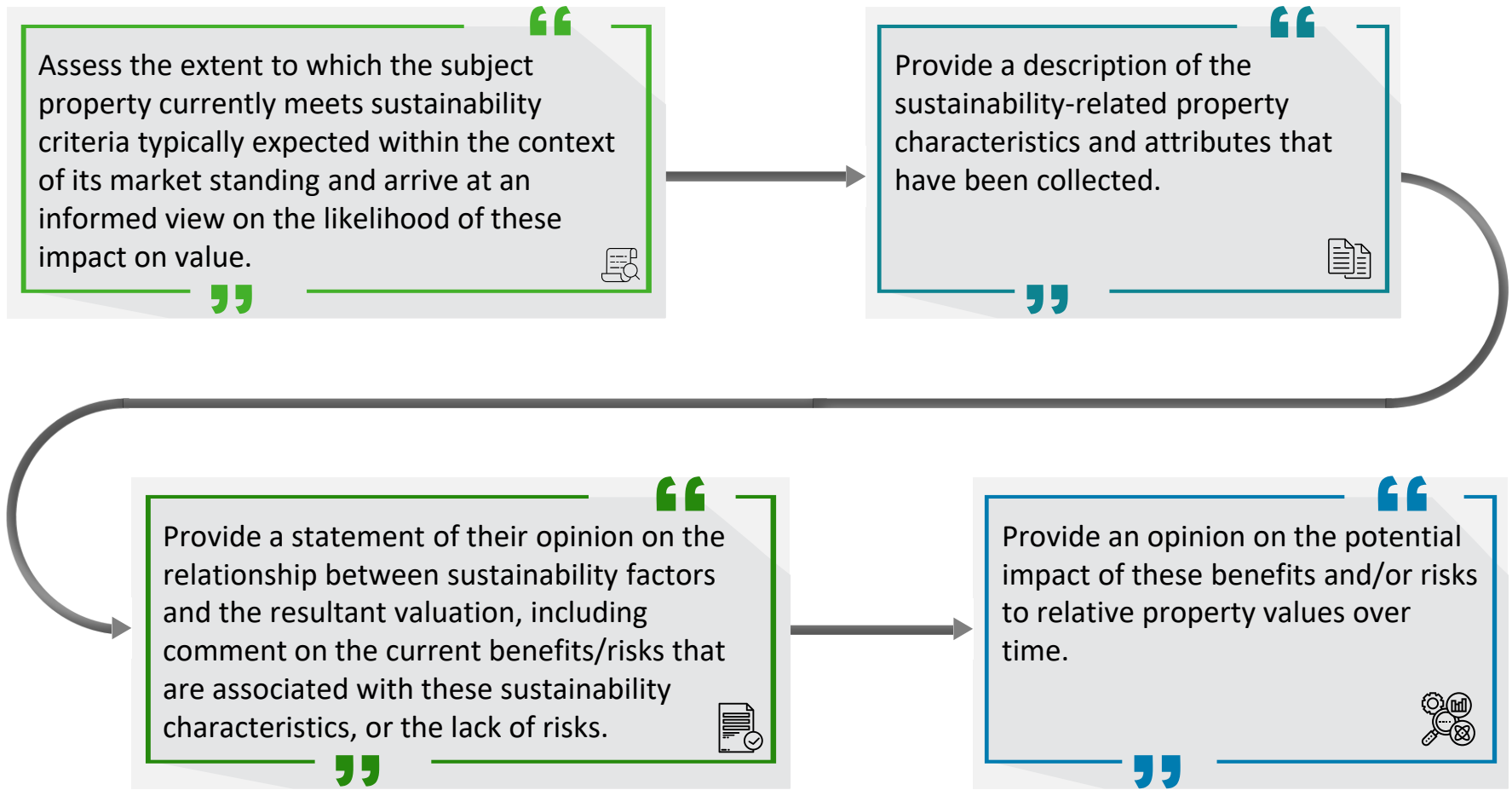
“Where appropriate, in order to comply with best practice in reporting, valuers are recommended to:

- **Assess** the extent to which the subject property currently meets sustainability criteria typically expected within the context of its market...
- Provide a **description** of the sustainability-related property characteristics...
- Provide a statement of their opinion on the **relationship** between sustainability factors and the resultant valuation...
- Provide an opinion on the **potential impact** of these benefits and/or risks to relative property values over time....”



RICS “ESG & Valuation” Guidance Note – Transparency & Disclosure

Adopted in January 2022, the Guidance Note’s primary aim is support valuers in being explicit in their identification and articulation of Sustainability & ESG issues, how they have influenced their thinking and to support the reporting process.



Source / Link to Guidance Note: [sustainability-and-esg-guidance-note_december-2021_v1.pdf \(rics.org\)](https://www.rics.org/valuation-and-esg-guidance-note-december-2021-v1.pdf)

Evolution in Valuer Engagement Letters

ESG is a rapidly evolving agenda requiring specialist skills. Valuers beware!

“With regard to EPCs, the valuer should provide an estimate of CapEx necessary for the property to meet current and future EPC targets.”

“The valuer should identify any risks related to the EPC and provide comment upon them.”

“The valuer must provide comment on the energy consumption in design, construction and usage of the building – including providing calculations of energy use intensity and embodied carbon for developments.”

The ESG agenda presents a unique opportunity for stakeholders across the Real Estate community to collaborate. However, there is a danger that progress will be stifled if an approach which seeks to “offload risk” or underestimate the extent of specialist expertise required is taken.

Valuers' "frame of reference" is changing....quickly

Data, Tools, KPIs and Market Dynamics are developing

The Valuer's "Shopping List and Toolkit" is evolving...



EPC information – publicly available:

<https://find-energy-certificate.digital.communities.gov.uk/find-a-non-domestic-certificate/search-by-postcode>



Certification information BREEAM, LEED, NABERS



Emerging tools such as "Paris Pathway" insight available through **Carbon Risk Real Estate Monitor (CRREM)**



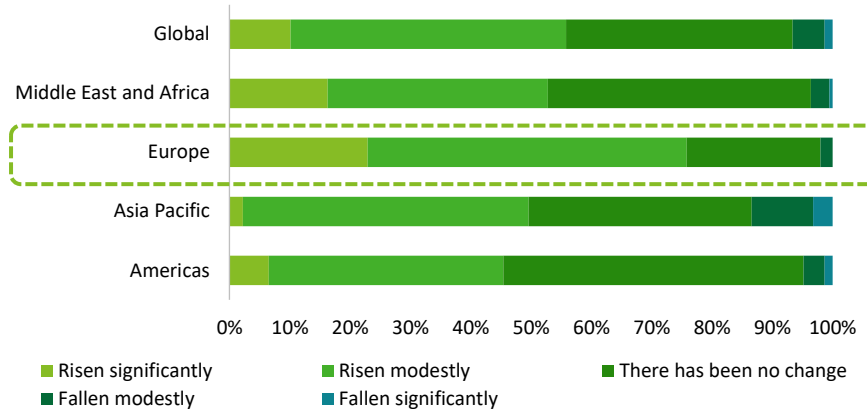
Better Buildings Partnership's **Education** programme



Numerous Consultant **research and insight** reports

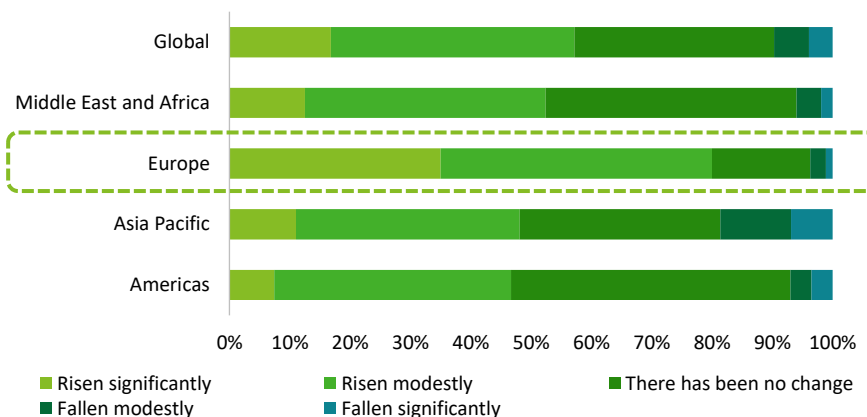
...as is the market

Change in Demand Amongst Occupiers



Source: RICS

Change in Demand Amongst Investors

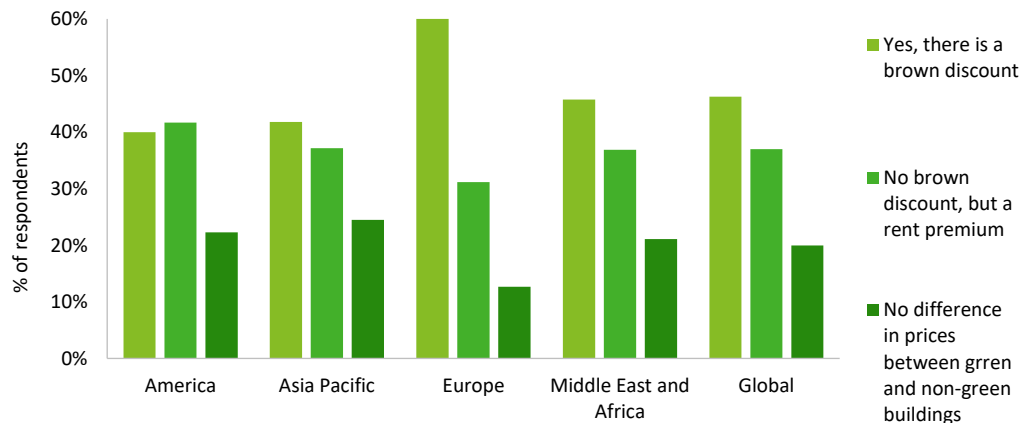


Source: RICS Sustainability Report 2022

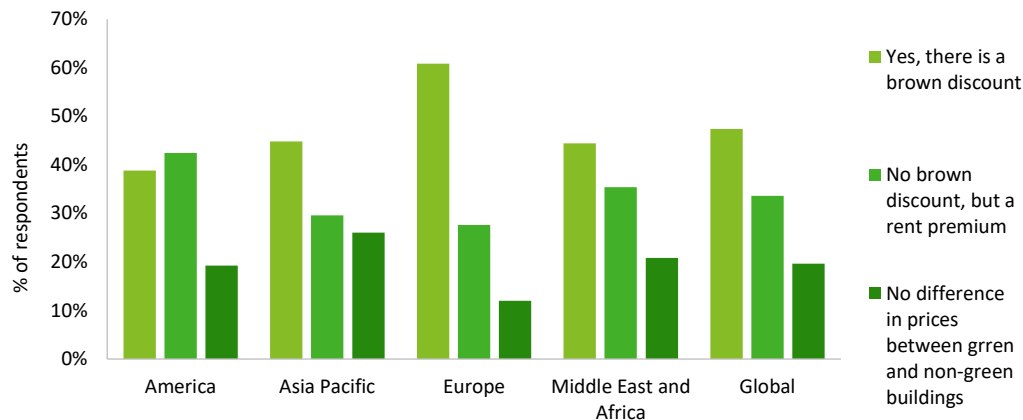
Sustainability is believed to be influencing Rents and Prices – now

Growing recognition/acceptance of the concept of “Brown Discount”

Rental Levels



Risk Pricing



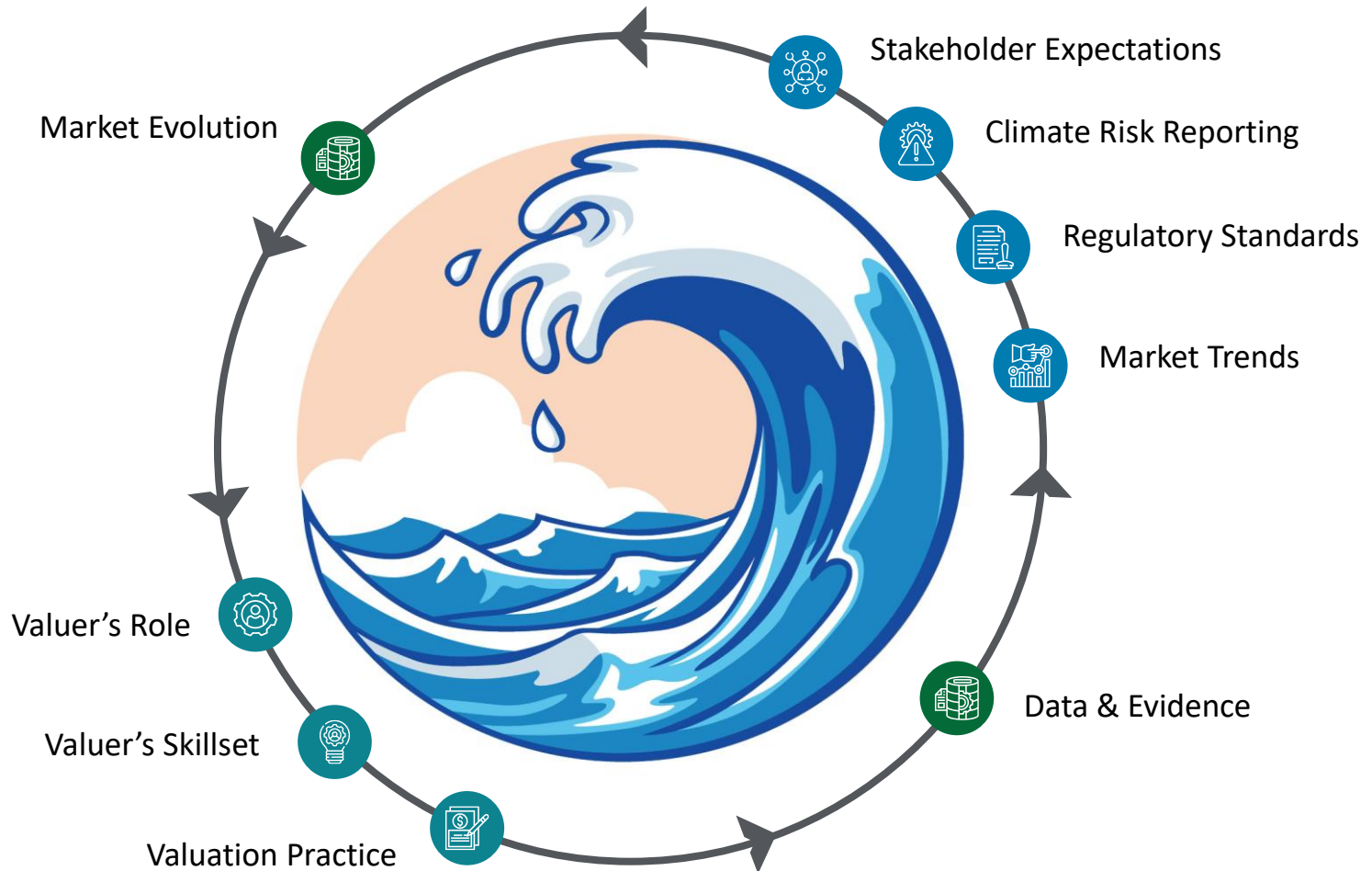
c. 90% in Europe

....believe there to be a rental differential

....believe there to be a “Risk Pricing” differential

To Conclude

The momentum – or tide – behind ever greater Transparency and Disclosure is set. Valuers can, and should, be playing a key role. Evidence and Data is emerging, but quantitative analysis is challenging and must not “get in the way” of progress.





This publication has been written in general terms and we recommend that you obtain professional advice before acting or refraining from action on any of the contents of this publication. Deloitte LLP accepts no liability for any loss occasioned to any person acting or refraining from action as a result of any material in this publication.

Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675 and its registered office at 1 New Street Square, London, EC4A 3HQ, United Kingdom.

Deloitte LLP is the United Kingdom affiliate of Deloitte NSE LLP, a member firm of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"). DTTL and each of its member firms are legally separate and independent entities. DTTL and Deloitte NSE LLP do not provide services to clients. Please see www.deloitte.com/about to learn more about our global network of member firms. Real Estate Services regulated by RICS.

© 2022 Deloitte LLP. All rights reserved.