

Basel Committee Secretariat
Basel Committee on Banking Supervision
Bank of International Settlements
CH-4002 Basel
Switzerland.

31 May 2001

Dear Sir or Madam

Response to the New Basel Capital Accord (Basel 2)

1. Introduction

We welcome this opportunity to comment on the New Basel Capital Accord (NBCA) published in January 2001. We would like to make clear that we limit our remarks to those areas of the NBCA that we perceive as relevant to the property profession.

RICS represents over 110,000 Chartered Surveyors worldwide and is regulated by its Charter with the objective of promoting the public good. This allows RICS to comment independently on matters that it perceives to be relevant to its profession. RICS members work in both the public and private sectors.

Valuation forms a significant part of the work of the profession, demonstrated by the fact that over 21,000 members of the RICS belong to its valuation faculty. A significant proportion of the work of those RICS members who specialise in valuation is performed for the banking community and RICS members are keen to develop their skills and services to meet these needs.

2. Background to RICS response

As a leading member of the International Valuation Standards Committee (IVSC) the RICS has sought to co-ordinate its comments with those of the IVSC. Accordingly we endorse the detailed comments made by the IVSC in its submission to the Basel Committee. However, we would lay particular emphasis on the points made below in paragraph 3. Both RICS and the IVSC recognize that, in an increasingly global economy, standardisation of economic practices is desirable and in support of this the RICS is keen to advocate the commonality of valuation practices. The importance of property as collateral for bank lending purposes makes greater harmonisation of valuation standards highly desirable.

The RICS convened a specialist Working Group to consider the proposals set out in the consultation exercise. Members of the Working Group are listed at Annex A. In drawing together these comments and the working group RICS drew on the international expertise

and experience of its members. Within the UK context, RICS consulted with the UK Government Department for the Environment, Transport and the Regions (DETR), responsible for property issues, the Bank of England and the Financial Services Authority.

3. Principal Comments

The Working Group considered the NBCA and each of the points that had been raised in the IVSC submission and concluded that they were in agreement with the issues examined, and the conclusions reached by IVSC. The RICS endorses the views made by IVSC and confirms these represent the views of the RICS membership in the context of achieving global standardisation in valuation practices, but in addition would stress the following points.

- Acknowledgement of International Valuation Standards.
The RICS has been a world leader in the development of valuation standards, which are contained in the RICS Appraisal and Valuation manual (known as the ‘Red Book’). With the increasingly global nature of business there is a need to develop internationally acceptable valuation standards in conjunction with other leading valuation bodies. The RICS plays a full and active part in this and, in the context of achieving an international agreement on banking regulatory practices, we support an international valuation standard.
- Adoption of the International definition of Market Value.
One of the earliest achievements in the development of international cooperation on valuation standards was agreement on a common definition of Market Value. This lies at the core of International Valuation Standards and is now widely incorporated in individual country standards. **We recommend strongly that this internationally accepted definition of Market Value replaces the definition currently employed by the NBCA.**
- Clarification of what constitutes Commercial Real Estate.
Commercial Real Estate is used repeatedly through Basel 2 but in different contexts and with different meanings and parameters. This makes interpretation of its proposals unclear and could lead to misunderstanding. RICS would be happy to advise on a suitable definition.
- Consideration of merits of Investment Grade Property as the optimal collateral.
Our enquiries have indicated that there appears to be a lack of adequate statistical data supporting the performance of loans subject to different categories of loan collateral. Intuitively we believe that income-producing investment property has the characteristics which make it a superior form of collateral to other types of commercial real estate. Through its national and international representations there may be opportunities for the RICS to contribute research data on property as loan collateral in support of Basel 2 proposals and we believe this is an important area requiring attention.
- Clarification of the eligibility for exceptional treatment.
The application of the exceptional treatment provisions is far from clear given the “fluid” definition applied to Corporate Real Estate and CRE lending.

- Establishment of a regular dialogue with the valuation profession in the mutual quest for improved standards.

Real estate is one of the major forms of collateral securing bank lending. As the profession specialising in the measurement of the value of that collateral, we consider it would be in the interests of both banking regulators and valuers to develop their professional standards in cognizance of each other.

- Mortgage lending value (MLV).

We consider that MLV is essentially a risk assessment technique rather than specifically a "valuation". Coupled with the somewhat unclear definition in the "exceptional treatment" we have concerns that this could lead to a lack of uniformity in approach by different organisations and / or valuers in countries outside its origins.

Notwithstanding, the inputs into this assessment are ones which valuers are well placed to derive.

We recommend that this approach be more clearly identified as a risk assessment technique and that the Committee consults with valuation organisations, including, International Valuation Standards Committee (IVSC), The European Group of Valuers' Associations (TEGoVA) and ourselves in order to give greater clarity to the definition and, if possible, an agreed commentary.

Many RICS members work both 'in-house' within banks and financial institutions and as external advisers to these institutions, in the measurement of property collateral. They are bound by the rules and standards of this Institution and we believe it is important that our regulatory rules are seen as complimentary to those of the rest of the financial community. It is for this reason that we have taken a close interest in the development of banking industry practices and, in particular, the development of the proposed New Basel Capital Accord.

I would be pleased to discuss any of the points raised in this submission at your convenience.

Yours faithfully



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Annex A**Members and Secretariat of RICS Working group on New Basel Capital Accord**

Position/representation	Members	Company
Chairman	Mr John Rich MA FRICS	Investment Consultant, IVSC
	Martin Brühl BSc MRICS	Healey & Baker, Frankfurt
(TEGOVA)	Peter Champness	LCS Associates, London
	Andrew Cherry FRICS	Healey & Baker, London
	K K Chui	DTZ Debenham Tie Leung, Hong Kong
	Nick French BSc MRICS	University of Reading
	Harvey Kasin FRICS	HVB Real Estate Capital Ltd., London
	Jim Morley	Barclays Bank, London
	Alastair Murdoch BA MRICS	HVB HypoVereinsbank, New York
	Andrew Renshaw BSc MRICS	Insignia Richard Ellis, London
	George Tonks	HSBC, Birmingham
Secretariat	Adrian Nelson MRICS	RICS Valuation Faculty
Secretariat	Jill Craig	Head of Policy RICS Brussels
Secretariat	David Melhuish	RICS Policy Unit, London

In addition comments were gratefully received from Herr Wolfgang Kalberer of Verband Deutscher Hypothekenbanken.

Glossary

FRICS	Fellow of the RICS
MRICS	Member of the RICS