POSITION PAPER

RICS Position Paper on Prudently Conservative Valuation Criteria in the Context of CRR Implementation in Europe

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1. Context and Regulatory Landscape

As Europe prepares for the implementation of the **Capital Requirements Regulation (CRR)** and **Basel 3.1 standards**, the introduction of a property valuation using prudently conservative valuation criteria[1] may end up representing a material change to real estate valuation practices. It is scheduled to take effect on 1 January 2025. We need to understand the implications of the new criteria for valuation practice to ensure consistency, transparency, and resilience across European real estate markets. RICS is committed to developing a consensus and subsequent guidance.

The property value undertaken using prudently conservative valuation criteria does not supplant market value as the main basis of valuation for loan origination and monitoring purposes. Instead, it represents a possible additional adjustment that a lender may need to make, if circumstances dictate, to the market value. In many circumstances the market value will be sufficient to address the four specific criteria set out in the CRR and Basel 3.1. It is therefore important to identify why these criteria have been formulated, what those circumstances might be, and how the criteria could be implemented. This position paper sets out RICS thinking on the issue and suggests what needs to be undertaken to take this matter forward.

With the implementation of prudently conservative valuation criteria, consistency emerges as a vital priority. A harmonized approach across Europe to the adjustment of market values for the criteria is critical to avoid the pitfalls of fragmented regulatory interpretations. Without uniformity, inconsistencies between national frameworks could result in regulatory arbitrage, diminished investor confidence, and potential market disruptions. To prevent these challenges, RICS advocates for the establishment of standards that ensure a cohesive application of prudently conservative valuation criteria. This includes a clear and transparent approach that enables all stakeholders to work within a predictable and stable framework. In Europe, achieving this goal relies on the collaboration of EU member states, the European Commission, and the European Banking Authority, alongside key European lender and valuer organizations such as the European Mortgage Federation (EMF) and the European Group of Valuers (TEGOVA).

The implementation of prudently conservative valuation criteria also raises fundamental questions about the nature of a valuation and any division of responsibility between regulators, lenders and valuation professionals. It is necessary to set out the criteria and place them within this context before any principles for assessing these criteria can be created.

As a key issue for implementation is consistency and the need for harmonization in how prudently conservative valuation criteria adjustments are applied across Europe, inconsistent application of the prudently conservative valuation criteria concept could lead to regulatory arbitrage, where certain markets or institutions might gain an advantage due to less conservative valuation standards. Therefore,

[1] Property value undertaken using prudently conservative valuation criteria can be also named Property Value/ Prudent Value/ Prudential Value.

it is essential that EU member states work closely with lenders, valuers, and regulators to ensure a uniform approach to prudently conservative valuation criteria across the region.
This harmonization effort requires the adoption of common standards across borders, which can be achieved through collaboration between national regulators and the banking industry. Clear guidelines from the European Commission and the European Banking Authority will ensure that real estate exposures are consistently evaluated, strengthening financial stability and reducing systemic risks.

This is also important globally and Europe should not develop solutions in isolation of other jurisdictions worldwide.

2. Core Principles of Prudently Conservative Valuation Criteria

With effect from 1 January 2025, Article 229 of the CRR indicates that the property valuation of immoveable property collateral must be appraised by an independent valuer, while also specifying additional requirements. These are:

- the value must exclude expectations of price increases;
- the value is adjusted for the potential for the current market value to be significantly above the value that would be sustainable over the life of the loan;
- the value is not higher than the market value (where this can be determined).

The criteria have not been explained within Basel 3. They are therefore very vague and have not been set out with any clear guidelines as to methodology or any detail of how they might be implemented, and very little on who is responsible for developing any methods.

It is therefore useful to look at the issues which led to these criteria. They are embedded in the global financial crisis and the role real estate played during the crisis. Many of the studies into the crisis identified a problem with over-lending within real estate markets in the latter stages of a major real estate market cyclical boom in the period 2004 to 2007, with no additional constraints on loan-to-value ratios in that period. These late-cycle real estate loans went into technical default in many countries following the major real estate price corrections in 2007-2009. Rather than let banks go under, Governments stepped in to shore up the banking system.

This identifies cyclical *market* movements as the main target for reform rather than *individual asset* issues which are picked up in mainstream market valuations. Much of the research and development behind prudently conservative valuation criteria has emphasised the difference between a property valuation, using objective definitions producing outcomes that can be measured against transaction prices, and a market analysis that puts those valuations/prices into a longer-term context as required by the criteria. It also identifies that cyclical movements are highly correlated across real estate sectors and markets.

Prudently conservative valuation criteria should therefore not be seen as a new valuation approach. Rather, it is a market level adjustment applied to the individual property market value to account for the long-term risks identified above.

To summarize, the primary purpose of the prudently conservative valuation criteria adjustment is to ensure property valuations remain reflective of long-term, sustainable “through the cycle” market trends. This concept contrasts with market value, which reflects the market at the date of valuation and tends to be more volatile and subject to short-term economic fluctuations. The task of the valuer remains the same; to identify the market valuation and to identify any specific asset issues which may affect the suitability of the individual property asset as security for a loan. The adjustment for any disequilibrium in real estate markets is a market analysis function which should be developed and applied independently of the individual asset valuation at a market or sub-market level.

3. The Role of Lenders and Valuers

One of the most critical aspects of implementing prudently conservative valuation criteria is determining how the adjustment is identified.

RICS believes that the adjustment to market value should be carried out following detailed guidelines including a prescribed methodology. This approach allows for some flexibility while ensuring consistency in how values are adjusted across different markets and institutions. The requirement for an independent valuation is covered by the individual asset market valuation and therefore does not necessarily mean independent from the lender organisation, just the loan making decision.

RICS believes that the guidance should come from the regulators in consultation with real estate lender and valuer organisations. Individual lenders should not be allowed to develop their own guidelines as the revised system has been developed to protect Governments and the public from unsustainable lending in late stage booming cyclical markets by those lenders. In addition to any inconsistencies between lenders, this is a conflict of interest.

Allowing individual valuers to identify cyclical market-based adjustment factors at the individual property asset level would be even more inconsistent and hold significant risks for both lenders and valuers, including significant cost issues.

At the time of writing there is no guidance from either regulators or lenders on how these adjustment factors are to be developed and implemented.

As Europe embraces this regulatory shift, it is worth noting the divergence in approach taken by the United Kingdom. The UK Prudential Regulation Authority has opted not to implement prudently conservative valuation criteria as part of its Basel 3.1 standards, citing the additional complexity it introduces to the valuation process. Instead, the UK relies on existing frameworks to address property-related risks. While this decision reflects a more simplified approach, it highlights the importance of ensuring that the EU’s prudently conservative valuation criteria framework is robust and capable of maintaining its credibility in the face of differing international standards. Moreover, the divergence underscores the need for ongoing dialogue to address potential challenges in cross-border lending and investment between the EU and the UK.

4. Recommendations for Industry Stakeholders

Looking ahead, RICS calls on all stakeholders to seize the opportunity presented by prudently conservative valuation criteria. As the January 2025 implementation deadline approaches, there is a pressing need for alignment in policies, practices, and expectations across the industry. RICS continues to advocate for the adoption of consistent guidelines to eliminate ambiguity, the fair allocation of responsibility to prevent disproportionate burdens on valuers, and the promotion of sustained dialogue among regulators, lenders, and valuation professionals. These steps are essential to ensure that prudently conservative valuation criteria not only meet regulatory requirements but also support the long-term health and stability of the European real estate market.

The introduction of prudently conservative valuation criteria under the CRR and Basel 3.1 standards marks a pivotal moment for the European real estate sector. If implemented thoughtfully and harmonized effectively, this adjustment can transform the property valuation into a tool for resilience and stability. RICS is proud to lead this effort, working alongside regulators and stakeholders to turn a regulatory obligation into an opportunity for growth, trust, and innovation. By setting a standard for prudently conservative valuation criteria that is clear, consistent, and robust, Europe can strengthen its financial systems while positioning the real estate sector as a cornerstone of sustainable economic development.

RICS remains committed to shaping the future of valuation standards and ensuring the European property market continues to thrive in an evolving regulatory landscape.

Delivering confidence

We are RICS. As a member-led chartered professional body working in the public interest, we uphold the highest technical and ethical standards.

We inspire professionalism, advance knowledge and support our members across global markets to make an effective contribution for the benefit of society. We independently regulate our members in the management of land, real estate. construction and infrastructure Our work with others supports their professional practice and pioneers a natural and built environment that is sustainable, resilient and inclusive for all.

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