

International Valuation Guidance Note No. 7

Consideration of Hazardous and Toxic Substances In Valuation

1.0 Introduction

- 1.1 The objective of this Guidance Note (GN) is to assist Valuers in preparing valuations when specific hazardous or toxic substances may influence property values.
- 1.2 Hazardous and toxic substances are included among a number of possible environmental factors that, when appropriate, are specifically considered by Valuers. This GN is limited to consideration of hazardous and toxic substances because other environmental factors that may be encountered in valuations typically have less involvement with scientific and associated technical issues, including related law.
- 1.3 This GN addresses general concepts, principles, and considerations that guide Valuers in preparing valuations when hazardous or toxic materials that may influence property values are present. It also discusses concepts that must be understood by accountants, regulatory authorities, and other users of valuation services.
- 1.4 Valuers rarely have special qualifications in legal, scientific, or other technical areas that involve evaluating risks associated with hazardous or toxic substances. When considering the market effects of such risks in property valuations, Valuers commonly rely upon other experts' advice. As specified in International Valuation Standard 1 (IVS 1), significant reliance upon other experts' advice must be disclosed and explained in the context of the property addressed in the Valuation Report.
- 1.5 Fundamental to the application of this GN are the Valuer's adherence to market-based valuations, objectivity, and full disclosure of relevant matters. Similarly, Valuers are obliged to write Valuation Reports that may be reasonably understood by clients and others. The obligation for clarity and full disclosure is particularly important

when scientific, technical, and legal issues are involved.

- 1.6 This GN also provides for proper treatment and disclosure of hazardous and toxic substance issues when valuing specialised properties and in other situations, which preclude the application of *Market Value* concepts.

2.0 Scope

- 2.1 This GN applies to all valuations of property including plant and equipment. Special provisions of the GN should be observed when hazardous or toxic substances that may influence the property's *Market Value* or other defined value are known or reasonably believed to be present.
- 2.2 Legislative, regulatory, or accounting requirements, or those of a legal jurisdiction, may oblige modification to this GN in some States or under certain conditions.

3.0 Definitions

- 3.1 *Hazardous or toxic substances* within the context of this GN involve specific materials that, by their presence or proximity, may have adverse effect on property value because of their potential to cause harm to life-forms. Such materials may be incorporated into improvements to or on the site, or they may be found in or on the land. They may also be offsite, but nearby. In some instances they may be airborne.
 - 3.1.1 In a more general use beyond this GN, *environmental factors* may be characterized as influences external to the property being valued which may have positive effect, negative effect, or no effect at all on the property's value. Hazardous or toxic substances may be found either on or off the site of the property valued.
- 3.2 *Hazardous substance* within the context of a valuation is any material within, around, or near the property being valued that has sufficient form, quantity, and bio-availability to create a negative impact on the property's *Market Value*.

- 3.3 *Toxic* describes the status of a material, whether gas, liquid, or solid, that in its form, quantity, and location at the date of valuation has capacity to cause harm to life-forms. *Toxicity* refers to the degree or extent of such capacity.

4.0 Relationship to Accounting Standards

- 4.1 While the expressions *Market Value* and *Fair Value* may not always be synonymous (see International Valuation Standards 1 and 2 [IVS 1 and 2] and International Valuation Application 1 [IVA 1]), each type of value reflects market behaviour under conditions contained within the respective definitions. To the extent that property values reported under either type of value may be affected by hazardous or toxic substances, proper disclosure and the application of proper valuation procedures to the circumstances are necessary in making and reporting valuations.
- 4.2 This GN is applicable to all circumstances involving public disclosure of property values, whether reported individually or in the aggregate, when hazardous or toxic substances may have adverse effect on such values. In addition to the possible effect of such considerations on the properties valued, it is possible that there are other accompanying issues such as curative or restoration costs, maintenance or monitoring costs, third-party or regulatory liabilities, and the like. Thus, proper disclosure and handling are essential in valuations used for preparation of financial statements and related accounts.
- 4.3 In the ordinary course of conducting an asset valuation, the Valuer will be instructed by the Directors of the enterprise/entity as provided in IVA 1. Any special instructions to the Valuer concerning the handling of hazardous or toxic substance issues that may have negative impact upon property value are, under IVA 1, important disclosures to be discussed by the Valuer in the Valuation Report. Such disclosures shall be accompanied by the Valuer's explanation of how the issues are handled in the Valuation Process; any assumptions that are made; and the effect, if any, such considerations have upon the value reported.
- 4.4 Although the value effects of hazardous or toxic substances are derived from the market in a *Market Value* assignment, such effects

may not be as readily discerned when valuing property for which a *Depreciated Replacement Cost* method is appropriate. To comply with IVA 1 when applying the DRC method, Valuers should apply the principles of this GN to the extent possible and should fully disclose the extent of their analysis and the basis for their conclusions.

- 4.5 The accounting definition of *impairment loss* is the amount by which the carrying amount of an asset exceeds its recoverable amount (IAS 36, para. 5). The negative impact of hazardous or toxic materials that are present in a property may contribute to its impairment. The impairment loss incurred by a property where such substances are present may include the adverse effect of those substances upon property value. (See para. 5.4 below.)

5.0 Guidance

- 5.1 **In dealing with a client or prospective client in matters pertaining to the valuation of property when known or reasonably discoverable environmental conditions that may have adverse influence on property values are present, the Valuer should disclose to the client the extent of his or her knowledge, experience, and competency to deal with the situation.**

5.1.1 If the environmental factors are known or are suspected to exist at the time the Valuer and prospective client are discussing the potential engagement, the Valuer should satisfy himself or herself that the client understands the Valuer's competency and disclosure obligations and that undertaking the engagement will in no way compromise these obligations.

5.1.2 If the environmental factors are discovered after commencing the engagement, the Valuer should make known to the client the knowledge, experience, and competency disclosures specified by this Guidance, and should then comply with all other IVS disclosure requirements.

- 5.2 **Recognising that many environmental situations will require advice on physical, legal, scientific, and other technical issues, if the engagement is otherwise acceptable to both the client and the**

Valuer, the Valuer should take the necessary steps to complete the assignment competently. These steps may include appropriate personal study; association with another Valuer who has the requisite knowledge, experience, and competency; or obtaining the professional assistance of others who possess the requisite knowledge, experience, and competency.

- 5.3 **Disclosure of the existence of any hazardous or toxic substance that may have adverse effect upon a property's value is included among the general reporting requirements of IVS 1, 2, and 3. Also required is the Valuer's disclosure regarding how that factor has been dealt with in the engagement.** If the engagement calls for valuation of the property as though no such environmental factor existed, full disclosure must be made of the limiting assumption, and reporting must comply with the statements above. (See para. 5.1 and 5.2.) **The requirements for valuation reports are addressed in the Code of Conduct and IVS 3, Valuation Reporting.**
- 5.4 **Where impairment is present in a property, the Valuer should estimate the value of the property as if the impairment had been removed. Where possible, the Valuer should identify the cost of remediation; but if this is not possible, the Valuer should disclose the fact that the property is impaired.**
- 5.5 **If a property is valued as if unaffected by hazardous substances, and such substances are known or suspected to exist, the Valuation Report should contain a qualification that clearly limits the scope of the valuation, an appropriate statement of purpose, properly qualified conclusions, and a restriction against use of the valuation conclusion without accompanying disclosure of the qualification and its explanation.**
- 5.6 **The names and nature of expert assistance of others who contributed specific information concerning effects of environmental factors on the property valued should be acknowledged in the Valuation Report.**
- 5.7 **When there are no known environmental factors that may have adverse effect on property value, the Valuer should, as a matter of routine practice, include within the Valuation Report a con-**

tingent and limiting condition or other disclaimer affirming that the valuation was made on the assumption that no such factors were known to exist at the date of valuation, but if such factors did exist they could well have an adverse effect on value.

- 5.8 There is growing worldwide concern about the effects of hazardous and toxic substances upon lives and property. Many potential hazards have been recently identified, and others are likely to be added over time as new and additional discoveries are made and subsequent controls are invoked by governments or are required by the market.
- 5.9 Some hazardous or toxic substances can have material effect on property values. However, **as Valuers normally deal with *Market Values*, it is the market's reaction to these substances that is at issue in *Market Value* engagements.** Over time, substances once believed to have no adverse effect on property value may be determined to have such an effect. Conversely, materials once believed to have substantial effect may be found to have little or no property value effect, or to have such effect only under certain market conditions.
- 5.10 The handling of physical, legal, scientific, and technical issues involved with hazardous or toxic substances is frequently beyond the skill of the Valuer. However, **the Valuer's role in consideration of such factors will be facilitated if**
- 5.10.1 **situations involving environmentally sensitive substances are recognised and dealt with in accordance with this Guidance**, whether they are encountered prior to undertaking an engagement or subsequent to its commencement;
 - 5.10.2 **proper reliance is placed upon the professional advice and assistance of others when special skills, knowledge, training, and experience are required, and any such assistance is acknowledged and explained in the Valuation Report;**
 - 5.10.3 **proper treatment is given to the influence of hazardous or toxic substances in the Valuation Process, or alternatively, if the Valuation Process is to exclude consideration of**

such matters, proper disclosure is made of any assumptions made, the purpose of the analysis, and the likely effect of the assumptions on the defined value;

- 5.10.4 **reasonable effort is made to ensure that reports and the value estimates they contain are not misleading and can be reasonably used only for the purpose for which they are intended.**
- 5.11 Valuers are expected to correctly apply those recognised methods and techniques that are necessary to comply with this Guidance. When valuing property subject to some hazardous or toxic substance that adversely influences property value, the Valuer should apply those processes necessary to adequately reflect any such value losses, taking care to neither over- or understate the value effects. **In a *Market Value* engagement, it is the Valuer's responsibility to reflect the market effect of the particular condition or circumstance.**
- 5.12 Valuers are cautioned that there can be considerable controversy among legal, scientific, and other technical experts upon whose advice the Valuer may need to rely. Particular differences may be found in the methods experts use to determine the extent of clean-up, maintenance, or monitoring that may be associated with hazardous or toxic substances and the costs required to accomplish such clean-up, maintenance, or monitoring.
- 5.12.1 **Engagements may require valuation of the affected property under an assumption that any value effect of the hazardous or toxic substances is excluded from the reported value.** Such engagements are acceptable, provided that the resulting valuation is not misleading, that the client is informed of and agrees to this limiting assumption, and that the Valuation Report clearly sets forth the limitation and the reasons therefore.
- 5.12.2 Because of technical issues frequently involved in environmental matters, it is common for Valuers, directly or through the client, to seek the counsel of and rely upon the opinions

of those who hold appropriate qualifications to evaluate problems involving hazardous or toxic substances. **Valuers should disclose the level and nature of reliance placed upon such opinions.**

- 5.13 Valuers and users of valuation services should recognise that the effect of a particular hazardous or toxic substance may vary widely with differences in properties, locations, and markets. Adverse value effects may range from none to those that are more than costs of cure and remediation. The latter may occur, for example, where *highest and best use* of the property affected is changed by the condition and where marketability or other usefulness of the property is altered. In any case, **it is the role of the Valuer to research and reflect the effects of the environmental factor on a particular property in its market.**
- 5.14 In the typical valuation engagement, the Valuer will not have the skills to make legal, scientific, or technical findings regarding hazardous or toxic substances, or other environmental factors that may have adverse effect on value. **It is important** to the credibility and usefulness of the reported value **that if any such conditions exist, they be properly considered and reported.**
- 5.14.1 **When the Valuer knows that a hazardous or toxic substance is present in the property specified in a valuation engagement, the Valuer should follow all requirements of this Guidance.** Normally, any technical experts upon whose advice the Valuer may rely will be engaged by the client or by others.
- 5.14.2 **When the Valuer has some reason to believe that a potentially adverse hazardous or toxic substance may be present, the Valuer should immediately make the client aware of the concern and request that the client take steps to resolve pertinent questions.** By handling this concern on a private, confidential basis, the Valuer keeps information confidential that in itself could affect the property involved.
- 5.15 Guidelines for Valuers' responsibilities to observe, locate, and identify hazardous or toxic substances or circumstances may vary from

time to time within and among jurisdictions. In general, determination of the nature, extent, and physical effects of environmental conditions is beyond the scope of service of Valuers.

5.16 In dealing with hazardous or toxic substances, the Valuer should research all related issues in a confidential manner so as not to raise undue speculation concerning the property.

5.17 It is not uncommon for individuals unfamiliar with hazardous or toxic substances issues to assume that if there is a physical effect of such substances, there must be an adverse economic reaction. Market experience shows there can be, and frequently are, important differences between general public perceptions and actual market effects of the presence of such substances. **The Valuer's role is to avoid such generally held but possibly erroneous assumptions and to carefully consider all significant factors, perform competent market research, and reflect relevant market attitudes towards the situation in Valuation Reports.**

6.0 Effective Date

6.1 This International Valuation Guidance Note became effective 19 April 1996.

