European Valuation Standards 2025
EVS 6 - Valuation and Energy Efficiency

Krzysztof Grzesik REV FRICS
Chairman TEGOVA

EUROPEAN VALUATION CONFERENCE

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Vancouver Valuation Accord March 2007

- The Accord was a commitment to work towards embedding sustainability within valuation practices, thereby 'mainstreaming' sustainability.
- Sustainability defined as "*development that meets the needs of the present without compromising the ability of future generations to meet their own needs*." This definition was supported by further explanation, noted in several United Nations texts, as being the "*interdependent and mutually reinforcing pillars of sustainable development – economic development, social development, and environmental protection.*"
- Agreed by amongst others: TEGOVA, RICS, Appraisal Institute of Canada, The Appraisal Institute, The Appraisal Foundation, Australian Property Institute.

But does anyone still remember ?

Fast Forward to Today and Lots of Noise about ESG

- **Energy efficiency**
- Renewable energy
- **European Green Deal**
- **Net Zero**
- Rooftop solar energy installations
- The greening of parking areas
- Legislation on air, water and soil
- The greening of construction materials and technical building systems
- Buildings in the circular economy
- EU taxonomy
- Green mortgages
- and financial institutions' and other industries' ESG obligations

Impact on Valuation of Real Estate

How is the valuer to make sense of EU Law and the wider complexities of ESG (Environment, Social, Governance) ?

Key Factors:

- The degree of coercion of the law
- Identifiable impact on real estate markets
- The scale and speed of impact

Taken together, they lead to a **two-tier approach**, *because there is a fundamental difference between the latest Green Deal energy efficiency EU legislation and all the rest.*

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First Tier Valuation Approach Energy Efficiency

The European Green Deal legislative package has several laws impacting buildings but two of them – by accelerating the speed and depth of renovation across Europe – have direct and rapid impact on markets and values:

1. The Energy Efficiency Directive

2. The Energy Performance of Buildings Directive

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Energy Efficiency Directive - (EU) 2023/1791
Exemplary role of public bodies' buildings

- 3% of buildings owned by **public bodies** must be renovated each year to nearly-zero energy building (NZEB) level.
- **Buildings rented by government from private sector landlords:**

Requires agreement with the owner, at lease renewal, change of use, significant repair or maintenance work, aiming for a nearly zero-energy building."

'**Nearly zero-energy building**' *means a building where the nearly zero or very low amount of energy is covered to a very significant extent by energy from renewable resources, including energy from renewable resources produced on-site or nearby (more detail in the Directive).*

Energy Performance of Buildings Directive

An EU law mandating how and by when renovation will have to be done affecting millions of homes, offices and shops at the same time.

All new buildings to be *zero-emission by* 2030 (new public buildings by 2028)

'Zero-emission building' *means a building requiring zero or a very low amount of energy, producing zero on-site carbon emissions from fossil fuels and producing zero or a very low amount of operational greenhouse gas emissions* (more detail in the Directive).

Compliance will mostly be checked on the basis of ***energy performance certificates*** (EPCs).

Energy Performance of Buildings Directive (2)

And in relation to **existing buildings**:

- **non-residential sector,** leading to the renovation of the 16% worst-performing buildings by 2030 and the 25% worst-performing buildings by 2033.
- **residential**, member states must establish a national trajectory that leads to reducing the average primary energy use of the residential building stock by 16% by 2030 and by a range of 20-22% by 2035.

EVS 6 (EVS 2020) Valuation and Energy Efficiency

A legal obligation to renovate a building to a higher level of energy efficiency by a fixed date or at a certain inflection point (e.g. rental, sale) creates an unavoidable major cost that impacts Market Value, as the owner at that date or inflection point will have to pay for renovation works.

Valuers must be aware of these legal deadlines and inflection points and …estimate the cost of a renovation deep enough to meet the required new level of energy efficiency … and consider the extent to which these costs affect the Market Value at the date of valuation.

EVS 2025
An Enhanced EVS 6 with Commentary on Valuation Methodology

Valuers will have to estimate the impact on market value of a building having to be renovated or, if it isn't renovated, not being sellable or rentable by a certain date.

If there is a statutory deadline affecting legal rights of use or disposal of a building unless it is at a certain EPC class, the valuer should use the residual method (residual approach?) to determine the Market Value, proceeding as follows:

a) Compare the building's EPC class with the class required by law at the next trigger point for that specific building .

b) Estimate the Market Value of the property after the renovation to reach the required EPC class by comparing with similar properties at that EPC class.

c) Using the residual method (residual approach), from the above end value obtain and deduct the cost of renovating to the required EPC class.

d) Deduct other costs including the cost of financing, professional fees and a developer's profit if appropriate.

A Modified Residual Method in Context of EVS 6

The residual method is described in the methodology section of EVS 2025. EVS 6 modifies the classic residual method by allowing for flexibility as to which costs should be deducted in addition to the cost of renovation. To summarise:

Estimate End Value of completed renovation

Deduct:

- **Costs of renovation**
- ***other costs including the cost of financing, professional fees and a developer's profit if appropriate***.

Thus in the valuation of an apartment having regard to local market practice and valuer's judgement, it may be appropriate not to deduct all of the above listed costs but a full residual calculation will normally be required in the case of large commercial property (office building, shopping centre, hotel etc)

Second Tier Valuation Approach:

The gradual valuation impacts of sustainability issues and ESG

Other EU Green Deal legislation is neither as coercive, as identifiable and quantifiable, nor as immediate in its effect as the energy efficiency laws.

Diverse sustainability factors going well beyond energy efficiency are *gradually* generating public consciousness of sustainability-induced investment risks and opportunities that most definitely impact perceptions of value.

Valuers need to recognise that and bring it to the attention of their clients.

But the mistake is to pretend that valuers can consider all these complex issues in the context of a standard valuation report.

Recognition of Two-Tier Approach in EVS 2025

European Valuation *Standard* 6 "Valuation and Energy Efficiency" is being improved and *enhanced with Commentary providing more detail on methodology*.

EVS Part III Valuation and Sustainability is being adapted to cover and *explain* all the new EU sustainability and ESG rules so that valuers are guided on the wider regulatory and market phenomena gradually transforming real estate markets and values.

THANK YOU!

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