



CENTRAL BANK OF
MONTENEGRO

Banking Supervision Department

GUIDELINES ON THE SELECTION OF VALUERS HIRED TO CARRY OUT ASSET QUALITY REVIEW

Definitions

AQR – asset quality review;

Guidelines – Guidelines on the Selection of Valuers Hired to Carry out Asset Quality Review;

AQR Manual – CBCG Asset Quality Review Manual submitted by the CBCG advisors, and drafted against the background of the Asset Quality Review Phase 2 Manual the European Central Bank's document of June 2018, adjusted to local specificities;

Workblock – an expression used to denote a working entity i.e. a phase of the entire process, all in accordance with the AQR Manual;

Potential valuers – valuers eligible in line with item 2 of these Guidelines;

AQR valuer – valuers selected by the AQR auditor;

Introduction

The Guidelines on the Selection of Valuers Hired to Carry out Asset Quality Review (hereinafter: the Guidelines) include initial instructions that apply in the process of selecting potential valuers for bank collateral, in connection with the AQR Workblock 5 implementation planned for 2020, all in accordance with the CBCG Asset Quality Review Manual (hereinafter: AQR Manual);

Potential auditors shall be eligible. Their eligibility shall be determined in accordance with item 2 of these Guidelines.

The AQR auditor is free to select one or more AQR valuers from potential valuers, taking into account the technical and financial aspects of the bids received, while considering and respecting the requirements of these Guidelines. For practical reasons, in these Guidelines, the AQR valuer will be stated in the singular form.

The AQR valuer shall be responsible for providing the necessary safeguards to ensure the independence of the appraisal. In order to ensure such independence, in cases of collateral previously assessed by the AQR valuer,



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and when that appraisal is not in accordance with the AQR Manual, the collateral shall be assessed by another valuer.

In its contractual relation with the AQR valuers, the auditor shall secure the possibility to, as appropriate or in accordance with the CBCG order, obtain all necessary data and information, insight into the details of the selection and activities of the AQR valuer on this project, as well as terminate the contractual relation in cases envisaged in the AQR Manual that primarily relate to inadequate provision of services by the AQR valuer.

Item 1

Key tasks of AQR valuers for valuation of collateral in line with AQR Manual

The key tasks relate to reviewing appraisals and, if necessary, conducting valuations of bank's collateral - real estate that is part of a sample of assets that will include apartments, office buildings, business facilities, ongoing investments, all types of land and other collateral subject to assessment. Such appraisals should be conducted based on a market value as a basis for valuation, in accordance with internationally accepted best practices, such as the European Valuation Standards, the so-called Blue Book (EVS 2016), then the Red Book issued by the Royal Institution of Chartered Surveyors (RICS), as well as International Valuation Standards (IVS 2017). In situations where there is a difference in the application of the methodology, the Blue Book standards shall prevail (EVS 2016).

The use of such valuation of collateral is performed with a view to verifying the correctness of data, as well as the accuracy and timeliness of valuation of collateral provided by the bank as input information for the implementation of AQR.

Even though it is envisaged that the main tasks of AQR valuers regarding the valuation of collateral appraisal is to focus on assessing the value of collateral in Montenegro, AQR valuers may also be required to appraise any assets held by a bank as collateral in other countries. The AQR valuer undertakes to conduct market appraisals in foreign countries if necessary, that is to provide their appraisal in accordance with these Guidelines and the AQR Manual, with the prior consent of the CBCG through third parties - valuers who must meet the same requirements as AQR valuers.

In cases of valuation of collateral related to uncollected loans, as well as in the case of assets acquired through collection of receivables, the AQR valuer shall visit the subject of appraisal and conduct an on-site visit, in accordance with the provisions of the AQR Manual.



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Item 2

Eligibility of valuers

Eligible valuers must:

- be registered to perform the relevant activity on the Montenegrin market according to the relevant local laws and subordinate legislation;
- meet the minimum eligibility requirements given in the following text;
- meet the conditions regarding restrictions given in the following text.

Minimum eligibility requirements that AQR valuers must meet

- The eligible valuer has had relevant engagements, i.e. valuations of bank collateral in the last five (5) years, looking back from the date of bid submission;
- The eligible entity or a consortium of valuers shall have full-time valuers with Recognized European Valuer REV (TEGoVA) certification or MRICS RV certification (Member of the Royal Institution of Chartered Surveyors, Registered Valuer);
- The qualified entity or a consortium of valuers shall have sufficient capacity, and a minimum of 5 employees for appraisal activities, to complete AQR Workblock5, within the deadlines defined in the AQR or Workblock 5 timeframe and at a satisfactory level, as defined in the AQR Manual to be submitted by the CBCG Advisor.

Limitations for valuers

The following eligible entities cannot be selected as bank valuers, if:

- Eligible entities or in the case of a consortium all involved companies/valuers cumulatively appraised more than 20% of the bank's portfolio collateral as at 31 December 2019;
- They performed appraisal services for the bank during 2019 and 2020;
- Eligible entity or a consortium of valuers are in the conflict of interest with the bank on the following grounds:
 - They are connected with the bank, i.e. the member of the banking group;



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- Responsible persons, as well as members of their immediate family, have a direct or indirect financial interest arising from the business relationship with the bank;
- Responsible persons, as well as members of their immediate family, hold managerial positions in the bank or the member of a banking group;
- Responsible persons, as well as members of their immediate family, have business relations through the provision of consulting services or on the basis of employment with the bank or the member of a banking group, or have an offer for such business relations from the parties in question;
- The amount of total annual fees borne by the bank for the appraisal services does not exceed the share of 25% in the valuer's annual income.

Minimum information to be submitted by valuers as proof of capability

For selection purposes, the valuers must submit at least the following information/evidence as proof of capability:

- Details of the composition and number of the proposed team (citing relevant experiences) together with résumés (i.e. CVs) and certificates/licenses of key staff who will take responsibility for the assigned tasks throughout the project;
- Evidence that the valuer has the capacity to value collateral in accordance with the European standards EVS 2016 (Blue Book) and other international standards, such as the guidelines of the Royal Institution for Certified Valuers (RICS - Red Book), where EVS 2016 takes precedence in case of any conflicts between different methodologies;
- Detailed project plan on how the applicant proposes the project to be carried out and how to address the tasks from Workblock 5 of the AQR process as defined in the AQR Manual;
- An analysis of the methodology detailing how the applicant will ensure that the schedule is respected and that a quality assurance process is established;
- Schedule of proposed fees by type of activity (appraisal review or preparation of a new appraisal) and type of appraised real estate;
- Valuer or AQR team of the bank are obliged to submit the results as part of T5 document, and at the request of regulator, the valuer is obliged to submit the relevant appraisal with all relevant evidence;



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- A description of how the valuer plans to ensure the confidentiality of data and results;
- If the valuer intends to use subcontractors, he must enclose a statement of his consent to participate, as well as the relevant licenses/certificates and CVs of team members. They must have the same qualifications and be subject to the conditions and restrictions set out in point 2 of these Guidelines.

Item 3

Results expected from valuers

Delivery of valuation results shall be prepared and submitted in line with the methodology established by the AQR Manual and instructions of the CBCG submitted during the AQR.

To avoid misunderstandings, valuations will be performed based on available documentation, and the AQR valuer is expected to use available data provided by the bank, which will include, but not limited to, previous valuations of the collateral. In special situations, the AQR valuer may visit the subject of appraisal, if deemed necessary, while in the case of collateral for uncollected loans and assets acquired through collection of receivables the valuer shall perform visit in accordance with the AQR Manual.

The final results to be submitted by the selected candidate must, in accordance with any additional requirements that the CBCG may issue from time to time, contain at least the following components:

- Introduction, description of appraised assets and summary;
- Work scope;
- Description of main limitations in the analysis;
- Valuation methodology and used assumptions;
- Conclusion on market value; and
- Detailed results and sources of information for each of the above stated tasks, and in particular for the assumptions used in the valuation, depending on the methodology used.



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Item 4

Quality control of performed valuations

All valuations shall be the subject of double quality control:

- The first quality control will be performed by a competent person on behalf of the AQR consultant performing the AQR in the bank;
- The second quality control will be performed by the CBCG team in charge of Workblock 5.

Both parties will have the right to dismiss the valuation as inadequate or to request a correction based on the standards against which the valuation should be performed.

Item 5

COVID-19 and business continuity plan

When drafting bids, the valuers are encouraged to present their internal procedures, capacities and ability to operate smoothly in stressful circumstances, as well as anticipated risks, which may arise in particular from a pandemic declared by the World Health Organization, caused by the outbreak of COVID-19.

The CBCG believes that although these are not mandatory requirements for valuers (and therefore not part of item 2), the banks should consider these characteristics in the selection process with a view to ensuring the highest possible level of business continuity in the given circumstances and conducting the AQR in a defined manner and within the defined deadlines.

Valuers are advised to implement recommendations of the TEGoVA Board of Directors given in the message concerning valuation during the Pandemic:

The pandemic has rendered real estate valuation work in most countries difficult to undertake in the absence of market activity (transactions are rare if not non-existent) as postulated by the definition of market value. In the circumstances many valuers have included disclaimer clauses in their reports highlighting the uncertain nature of the valuations reported. Whilst TEGoVA supports the insertion of such clauses, it is also aware that in some countries the law and standards may not allow them. Thus, valuers should ensure first and foremost that their reports are in compliance with local law.

TEGoVA also advises that where valuers are instructed to arrive at a market value of a property for a non-statutory purpose over the next few weeks:



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1) They should first identify the last date (pre-crisis date) when in their opinion a market value of the subject property could have been determined on the basis of the available market evidence and offer an opinion of the value of the subject property at that pre-crisis date. This will set a benchmark value against which the client can usefully gauge the market value reported at the relevant current date of valuation.

2) In reporting a value at a current date of valuation, valuers should make clear reference to the comparable evidence relied upon and state the extent to which adjustments if any have been made to that evidence on account of the crisis. If adjustments have been made, the valuer should justify them either on the basis of actual market evidence or reasoned valuer's judgement. Valuers are advised that for the duration of a period of market uncertainty in any particular local market they should not feel obliged to make adjustments (downward or upwards) to the pre-crisis market evidence provided this is made clear in the valuation report. In such a case the reported pre-crisis and current values will be the same subject to any material changes affecting the subject property between the two dates.

In following the advice set out in this communication, valuers should ensure that it is replicated in the Terms of Engagement agreed with the client. Valuers should also recommend that the value of the subject property be kept under frequent review.

Where local law prohibits the use of a disclaimer concerning "valuation uncertainty" or where a client instructs a valuer not to rely on such disclaimer, this should be noted in the Terms of Engagement agreed with the client.

The TEGoVA Board continues to monitor the situation and may issue further advice in due course. Also, valuers are advised to actively monitor TEGoVA recommendations and implement them in their work during the AQR process in line with the Manual.