# TECHNICAL MANUAL FOR THE DETERMINATION OF VALUE IN TERMS OF SECTION 12 OF THE PROPERTY VALUATION ACT 17 OF 2014 REVISED JANUARY 2020

OFFICE OF THE VALUER GENERAL

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## FOREWORD

The purpose of this manual is to provide general guidance to valuers who have been authorised by the Office of the Valuer-General to conduct valuations in terms of Section 12 (1) (a) of the Property Valuation Act No 17 of 2014. This section states that whenever a property has been identified for purposes of land reform, that property must be valued by the Office of the Valuer-General for purposes of determining the value of the property, having regard to the prescribed criteria, procedures and guidelines.

The value referred to, and defined in the Act, has its foundations in Section 25 (3) of the Constitution. This section prescribes that where someone has been deprived of property by the State, the amount of the compensation payable, and the time and manner of payment must be just and equitable, reflecting an equitable balance between the public interest and the interests of those affected. The section goes to state that in the determination of compensation, there must be regard to all relevant circumstances, including the current use of the property, the history of the acquisition and use of the property, the market value of the property, the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property, and the purpose of the acquisition.

The valuation of property that has been identified for purposes of land reform require professional valuers to apply the factors listed in the Constitution and in the Property Valuation Act. This manual aims to bring clarity regarding how valuers are to interpret these factors, and to arrive at a final determination of value. Recognising that the valuation of property is a well-defined and regulated professional activity, the manual does not take an overly prescriptive approach regarding what methods must be used. Valuers are expected to use their knowledge and professional judgment to deal with any specific valuation issues that may arise during their assignments. Rather, the primary intention of this manual is to ensure that all valuations done under the aegis of the Office of the Valuer-General are consistent, defensible, and in line with legislation.

The emphasis, therefore, is on adherence to the highest standards of professional practice. This professional ethos is critical to the work of Office of the Valuer-General, as the office begins to establish itself as an independent and professional institution, whose valuations are trusted and relied upon by all stakeholders in South Africa. In this regard, therefore, the manual is designed to be consistent with applicable International Valuation Standards, and similar exemplars of good professional practice. Any departures from these standards are only based on South African legislative and regulatory imperatives.

The manual is provided by the Office of the Valuer-General as a technical resource to the valuation profession in South Africa. It is meant to be a ‘living document’, to be regularly updated in response to changes in the legislative and professional environment, and in light of experience arising from implementation. Valuers are therefore encouraged to not only familiarise themselves with its contents, but also to provide any critical feedback, and to communicate this to the Office of the Valuer-General.

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**August 8, 2016**

## 1. INTRODUCTION

The purpose of this manual is to provide guidance to authorised valuers doing work on behalf of the Office of the Valuer-General (OVG), regarding procedures, techniques, standards and best practice regarding the determination of value for the purpose of Section 12 of the Property Valuation Act No.17 of 2014. The definition of value in the Property Valuation Act is consistent with, and gives practical effect to, the 'just and equitable' compensation requirement prescribed in Section 25(3) of the Constitution, and Section 12 of the new Expropriation Bill/Act.

The guidance provided in this manual does not take away from valuers their powers and responsibility to make appropriate professional judgments in each and every circumstance, and to apply generally recognised methods and procedures to the valuation of subject properties. The aim, rather, is to ensure that all valuations done under the provisions of the Property Valuation Act are consistent, comparable, defensible and in line with the Act and the Regulations. As such, the focus of the manual is on the application of general principles and procedures, rather than on valuation of specific types of property, or the application of different valuation methods. Valuers engaged to do work for the Office of the Valuer-General are expected to be competent and experienced in the use of all valuation methods, and on a wide variety of property types.

South Africa does not have a set of national valuation standards. Subject to the provisions of the Property Valuation Act and the Regulations to the Property Valuation Act, the guidance provided in this manual is consistent with, and draws from applicable and relevant International Valuation Standards. These are primarily the International Valuation Standards (IVS) produced by the International Valuation Standards Council (IVSC). Where the IVS are lacking, the standards of the Royal Institution of Chartered Surveyors (RICS) are used.

This manual is meant to be a living document and will be regularly updated in response to changes in the legislative, professional and socio-economic environment.

## 2. GLOSSARY OF TECHNICAL TERMS

"**acquiring authority**" means an organ of state seeking to make an acquisition of the subject property, including by way of expropriation

"**acquisition benefits**" means any benefits that accrued to the owner of, and the subject property, because of the manner of acquisition, including that they did not acquire the property at market value and from a willing owner, and where such acquisition and benefit was due to, aided by, or a consequence of past discriminatory laws and practices, or unlawful conduct

"**assumption**" means a supposition taken to be true and involves facts, conditions or situations affecting the subject of, or approach to, a valuation

''**authorised valuer''** means a registered valuer who has been authorised by the Valuer-General to conduct valuations in terms of section 11 of Property Valuation Act

"**current use value**" means the net present value, as at the date of valuation, of cash inflows and outflows, or other benefits and costs that the subject property generates for the specific owner in perpetuity or, in the case of a lease, to lease expiry, under lawful use, and without regard to its highest and best use, or the monetary amount that might be realised upon its sale

"**departure**" means special circumstances where the mandatory application of valuation standards may be inappropriate or impractical

"**depreciated replacement cost**" means the cost of obtaining an alternative asset of equivalent utility; this can either be a modern equivalent providing the same functionality or the cost of reproducing an exact replica of the subject asset, less total accumulated depreciation.

"**highest and best use**" means the reasonably probable and lawful use of property, that is physically possible, appropriately supported, and financially feasible, and that results in the highest value;

"**instructing authority**" means the department requiring a valuation of the subject property;

''**land reform''** means land redistribution, land restitution, land development and tenure reform

''**market value''** means the estimated amount for which the property should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion; Provided that in determining market value for purposes of section 12(1)(a) of the Property Valuation Act, prices paid by the State for any acquisition of property must be excluded; Provided further that in the even that no other credible data is available, prices paid by the State for any acquisition of property may be considered

"**net present value**" means the difference between the present value of cash inflows, or other benefits, and the present value of cash outflows, or other costs

**"net realisable value**" means the price of an asset that can be realised upon the sale of the asset, less a reasonable estimate of the costs associated with either the eventual sale or the disposal of the asset in question

''**property''** means—

(a) immovable property registered in the name of a person;

(b) any movable property which is contemplated to be acquired together with the relevant immovable property; and

(c) a right in or to such property, including an unregistered right recognised and protected by law;

"**Reasonably efficient operator**" means the assumption that the operator of a business conducted on the subject property is acting in an efficient manner, and involves the valuer estimating the trading potential rather than adopting the actual level of trade under the existing ownership;

''**registered valuer''** means a person registered in terms of the Property Valuers Profession Act as a Professional Valuer, Professional Associated Valuer or a specified category as a Public Sector Professional Associated Valuer;

"**regulations'**" means regulations made in terms of section 20 of the Property Valuation No. 17 of 2014;

"**special assumption"** means an assumption that either assumes facts that differ from the facts existing at the valuation date, or that would not be made by a typical market participant in a transaction on the valuation date;

"**subject property**" means the property which has been identified for valuation for–

(a) land reform purposes: or

(b) acquisition by a department, for any reason other than that mentioned in paragraph (a);

''valuation'' means the—

(a) process of estimating the value for a specific purpose of a particular interest in property at a particular moment in time; and

(b) outcome or result of the process referred to in this paragraph (a);

"**valuation basis**" means a statement of fundamental measurement principles or assumptions on which a valuation is premised;

"**valuation certificate**" means a summary valuation report containing inter alia, the following:

(a) legal description of the subject property;

(b) current use value of the subject property;

(c) value of acquisition benefits accruing to the owner;

(d) value of acquisition benefits accruing to the subject property;

(e) market value of the subject property;

(f) value of direct state investment in the acquisition of the subject property;

(g) value of direct state investment in the beneficial capital improvement of the subject property;

(h) value of the state subsidy in the acquisition of the subject property;

(i) value of the state subsidy in the beneficial capital improvement of the subject property;

(j) value of movable property on the subject property (if required);

(k) purpose of acquisition;

(l) overall value of the property as at the date of valuation, determined in terms of these regulations; and

(m) the identity and registration status of the authorised valuer.

''**Valuer-General''** means the individual appointed as Valuer-General in terms of section 8 of the Property Valuation Act, or acting as such;

"**valuation guidance notes**" means further information and material provided to assist in the application of valuation standards and for particular types of circumstances, and, while not mandatory for authorised valuers, are regarded as best practice;

"**valuation standards**" means statements of principles, guidelines and procedures that govern professional valuation practice and are mandatory for authorised valuers, subject to the provisions of any law;

## 3. THE LEGISLATIVE FRAMEWORK

### 3.1 The Constitution

The fundamental basis and support for the definition of value used in the Property Valuation Act is Section 25 (3) of the Constitution. Section 25 (3) of the Constitution states that:

- No one may be deprived of property except in terms of law of general application, and no law may permit arbitrary deprivation of property.
- Property may be expropriated only in terms of law of general application
  - for a public purpose or in the public interest; and
  - subject to compensation, the amount of which and the time and manner of payment of which have either been agreed to by those affected or decided or approved by a court.
- The amount of the compensation and the time and manner of payment must be just and equitable, reflecting an equitable balance between the public interest and the interests of those affected, having regard to all relevant circumstances, including
  - the current use of the property;
  - the history of the acquisition and use of the property;
  - the market value of the property;
  - the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property; and
  - the purpose of the expropriation.

- For the purposes of Section 25(3)
  - the public interest includes the nation's commitment to land reform, and to reforms to bring about equitable access to all South Africa's natural resources; and
  - property is not limited to land.

### 3.2 The Property Valuation Act No 17 of 2014.

The main purpose of the Property Valuation Act is to provide the State with institutional capacity to undertake valuations for land reform and other government purposes. The Act creates the Office of the Valuer-General and provides for its functions and powers. Of direct relevance to this manual is that it prescribes, in the principal legislation and the regulations, the criteria, procedures and guidelines for the valuation of property that has been identified for the purpose of land reform or acquisition or disposal by an organ of state.

This manual is a product of this legislation and embodies its prescriptions and guidelines. This manual lays out the procedures, guidelines and standards for determining the value of property for the purposes of section 12(1) (a) of the Property Valuation Act. This is defined in the legislation as the value of property identified for purposes of land reform, which must reflect an equitable balance between the public interest and the interests of those affected by the acquisition, having regard to all the relevant circumstances, including the

- current use of the property;
- history of the acquisition and the use of the property;
- market value of the property;
- extent of direct state investment and subsidy in the acquisition and beneficial;
- capital improvement of the property; and
- purpose of the acquisition.

The ‘value’ defined in the Property Valuation Act is clearly identical to ‘just and equitable’ compensation prescribed in both the constitution and the Expropriation Act/Bill. The difference in terms distinguishes between the technical process of determining economic value by professional valuers and the inherently judicial and political process of determining compensation to be actually paid in specific cases. The two processes are separate and distinct.

The responsibility of the Office of the Valuer-General is to objectively quantify the five prescribed factors as a critical input into the determination of just and equitable compensation by the relevant political authority and, where there is a dispute, by the courts. This distinction notwithstanding, the working assumption is that the value determined by the Office of the Valuer-General for the purposes of Section 12 of the Property Valuation Act will be equivalent to just and equitable compensation in terms of Section 25(3) of the Constitution and Section 12(1) of the Expropriation Act/Bill.

### 3.3 The Expropriation Bill/Act

The Expropriation Bill/Act is meant to be a law of general application as referred to in Section 25 (3) of the constitution. Section 12(1) of the Expropriation Act/Bill contains the provisions for the determination of compensation for property that has been expropriated. This section, which mirrors Section 25(3) of the constitution, provides that “the amount of compensation to be paid to an expropriated owner or expropriated holder must be just and equitable reflecting an equitable balance between the public interest and the interests of the expropriated owner or holder, having regard to all relevant circumstances, including

- the current use of the property;
- the history of the acquisition and use of the property;
- the market value of the property;
- the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property; and
- the purpose of the expropriation.

### 3.4 Restitution of Land Rights Act No 22 of 1994

This legislation has three key objectives. Firstly, it provides for the restitution of rights in land to persons or communities dispossessed of such rights after 19 June 1913 as a result of past racially discriminatory laws or practices. Secondly, it establishes a Commission on Restitution of Land Rights, whose main function is to facilitate land claims. Thirdly, it establishes a Land Claims Court whose main functions are to determine a right to restitution of any right in land in accordance with this Act and to determine or approve compensation payable in respect of land owned by or in the possession of a private person upon expropriation or acquisition of such land in terms of this Act, and to determine whether compensation or any other consideration received by any person at the time of any dispossession of a right in land was just and equitable.

The Restitution of Land Rights Act is directly relevant to the work of the Office of the Valuer-General and, by extension, that of authorised valuers. This is, firstly, because restitution of land rights might require acquisition, by negotiation or expropriation, of the rights of existing owners. This acquisition will be contingent on compensation which is 'just and equitable', in line with provisions of Section 25(3) of the Constitution. Even where restitution is by way of alternative land or monetary compensation, equivalence with the present value of the dispossessed land must be established on the basis of just and equitable compensation. Thus, a substantial volume of the work of the Office of the Valuer-General is going to arise from the application of this legislation.

Secondly, decisions of the Land Claims Court on matters of compensation are going to be binding, unless successfully appealed to the Constitutional Court. The Office of the Valuer-General thus has an interest in ensuring that valuations done in terms of this Act, and which may be precedent setting, are done with high degrees of professionalism and correctly, in accordance with the law.

## 4. THE CONCEPTUAL FRAMEWORK

As indicated above, the working assumption in this manual is that 'value' as defined in the Property Valuation Act is equivalent to 'just and equitable compensation' as provided for in Section 25(3) of the constitution. The central principle is that, as the constitution prescribes, the amount of compensation must reflect an equitable balance between the public interest and the interest of those affected. It is important to note that market value, and the assumption of willing-buyer willing-seller, is neither the basis nor the starting point of this approach.

Just and equitable compensation requires the balancing of the private right to full indemnity, on the basis of market value, and the public interest in having a successful land reform programme, among others. A balancing of interests is required because an insistence on the right to market value compensation will make land reform expensive, and possibly unaffordable. As Du Plessis (2009) points out, if the Government cannot pay the bill for land reform, it means that the dispossessed would not receive equitable redress, as section 25(8) of the constitution requires.

Implicit in the balancing act that is required for the determination of just and equitable compensation is a mutual assumption of costs. From the owner of the subject property's perspective, these relate to actual, or opportunity costs associated with the forfeiture of the right to full market value compensation. The State on the other hand, and as the constitution prescribes, is not entitled to acquire private property without the payment of a minimum level of compensation, consistent with the requirement of justice and equity. This payment must be made notwithstanding the unjust, irregular or violent manner by which some current owners, or their forbearers, acquired land. Without this mutual assumption of costs, the full cost of land reform will have to fall on one or the other party. This might mean that either the cost to the State will be too high for land reform to take place, or that few citizens would be required to bear a disproportionate burden for the public good. Neither of these outcomes would be just and equitable.

The notion of just and equitable compensation is closely associated with the idea of fairness. From a valuation profession point of view, the concept of 'fair value', therefore, provides an appropriate conceptual basis for the operationalisation of the principle of just and equitable compensation. Fair value is one of the four bases of valuation recognised by the International Valuation Standards Committee (IVS). The IVS defines fair value as "the estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties" (RICS, 2012, 31). The concept of fair value allows valuers to "estimate a price that would be fair in an exchange between two specific parties, without necessarily having to disregard criteria that would not be replicated in the wider market" (ibid.).

Fair value requires the assessment of a price that is fair between two identified parties considering the respective advantages or disadvantages that each will gain from the transaction (IVS). It is commonly applied in judicial contexts. Fair value is a broader concept than market value. Although in many cases the price that is fair between two parties will equate to that obtainable in the market, there will be cases where the assessment of fair value will involve taking into account matters that must be disregarded in the assessment of market value (IVS), such as the factors listed in section 25(3) of the constitution.

Conceptually, therefore, and in terms of IVS, authorised valuers are required to determine the fair value of the subject property, by taking into account the interests of owners on one hand, and that of the public, represented by the State, on the other. This balancing of interests between the parties has been codified in Section 25 (3) of the constitution. The fair value so determined will, in this context, be deemed to be equivalent with just and equitable compensation.

## 5. GENERAL VALUATION PROCEDURES

Due to the importance of the valuation process in the determination of just and equitable compensation, and the high likelihood of litigation, it is critical that the procedures followed, and decisions made by an authorised valuer in each and every case be meticulous and defensible. This requires, inter alia, strict adherence to prescribed procedure and the keeping of complete and accurate records, both for audit purposes and should they become required as part of a judicial process.

### 5.1 Instructions

An authorised Valuer may only undertake valuations on the basis of written instructions from an appropriate instructing authority. The instructing authority will in most cases be a government department, or in the case of authorised valuers who are in private practice, the Office of the Valuer-

General. An authorised Valuer must ensure that the written instructions conform to the prescripts of the regulations to the Property Valuation Act. These regulations require that the instructions must include the following information:

- a full description of the subject property;
- the details of the relevant legislation under which the acquisition is to be done;
- the purpose for which the subject property is required, and a statement that this is in the public interest or for a public purpose, as the case may be;
- the purpose of valuation;
- description of the interest or interests to be valued, and whether or not movable property, annual crops or growing timber, as appropriate, is to be included in the valuation;
- If movable property is to be included in the valuation, a full description thereof; and
- the effective date of valuation.

**5.2 Inspections, investigations and records**

Due to the complex nature of valuations to be done under the Property Valuation Act, and the high likelihood of litigation, a physical inspection of subject properties is mandatory. An authorised Valuer is required to ensure that due process is followed, by giving appropriate and adequate notice to the property owner(s) and/or occupiers and obtaining their consent and cooperation for the physical inspection.

5.2.1 Notice given by authorised Valuers

The authorised Valuer must deliver a written notice to the owner or person in charge of the subject property at least 7 days before the proposed date of physical inspection. The notice must include the following information:

- a full description of the subject property;
- the purpose of valuation;
- a description of the interest or interests to be valued, and whether or not movable property is to be included in the valuation;
- the extent and nature of the authorised Valuer’s planned investigations regarding the subject property;
- the nature of information that the authorised Valuer will require from the owner or person in charge of the subject property; and
- the dates and times that the authorised Valuer proposes to physically inspect the subject property.

5.2.2 Inspection and verification of information

Physical inspection of subject properties is mandatory in order for an authorised Valuer to verify all the relevant facts and circumstances affecting value. In summary, inspection is necessary in order for the valuer (1) to determine and record the nature and condition of the subject property, and to observe all factors which may affect its value, (2) to assess the comparability of the subject property with others, both in respect of its immediate use and its potentialities (3) to determine the highest and best use of the land and improvements.

Without being too prescriptive regarding procedures that all professional Valuers should be familiar with, it is important that the inspection is done meticulously and thoroughly. Bearing in mind that the Valuer may only have one opportunity for the exercise, the physical inspection should be carried out systematically, as follows:

**First,** preliminary work in the office should include search for title deeds, Surveyor General maps, zoning maps, rating rolls, etc. Before setting out for inspections, the Valuer should carry with him or her all the necessary tools, e.g. such as camera, distance measuring tools, town plan/street maps, papers, pencil or pen, etc.

**Second**, the general particulars of the region and the locality in which the subject property is found should be observed and recorded, namely, the proximity of towns, shops, schools, hospitals, etc. These are measures of accessibility to amenities and services and may have a lot of bearing on value. Distances to important amenities should be recorded.

**Third**, the particulars of the site or land on which the improvements stand should be examined carefully and recorded. This includes such items as access, road frontage, land size, shape and slope, fencing, gates, driveways, landscaping, availability of water, electricity, sewerage etc. The possible exposure of any type of property to such things as flooding, contamination, subsidence or problems from soil erosion is likely to have a considerable effect on value and must be recorded. In the case of agricultural property additional information will be required, such as soil condition, farm size, and type of crops grown in the area, topography, climatic conditions, utilisation of land, irrigation infrastructure, etc.

**Fourth**, the improvements on the land must be inspected and described. The Valuer may start from the exterior of the buildings and other improvements. The general description must focus on construction details of the main structure as well as the finishes, and their physical condition. The interiors of building must be examined room by room. Within each room the Valuer should normally start at the door, and then check the floor, windows, ceilings, fixtures and fittings, and taking dimensions appropriately, if there are no scaled building plans. If building plans are available, the Valuer should verify that these are in accordance with the reality on the ground, and any discrepancies noted. The Valuer should always be alert for any facts that might affect value, however small, such as damp walls, cracks, movements of the main structure etc. The inspection of the improvements must culminate in an "accommodation schedule' that must include details as the number of buildings, the number of rooms and their sizes and type of use.

**Fifth**, if movable property is to be valued as part of the instructions from an instructing authority, the Valuer must compile a list of all movable assets. The 'schedule of movable assets' must include details such as models, makes, serial numbers, dates of purchase, physical condition, mileages of vehicles, hours of tractors, etc.

**Sixth,** if growing crops and timber are to be included in the valuation, the Valuer should ascertain the date of planting or establishment, the type and variety of crops or timber, the area under cultivation, the stage in the life cycle, and the estimated date of harvest.

**Finally**, the owner, tenant or occupier of the property must be interviewed and/or required to provide such information as the Valuer might require for the valuation. The Regulations empower the Valuer to obtain information about the subject property relevant for the valuation, and that might reasonably be expected to be in the possession of the owner, tenant or occupier. This information includes, but is not limited to:

- purchase price and purchase date;
- nature of right transferred;
- discount rate and/or capitalisation rate;
- purchase and acquisition costs;
- financing terms;
- itemised annual revenues and expenses;
- financial statements;
- tenancy details (lease expiry dates, rents/royalties reserved and rent review terms);
- leasing costs, vacancies and collection losses;
- capital and maintenance costs;
- dates of completion of building works, and building plans;
- details of any acquisition benefits; and
- details of any direct state investment and subsidy in the acquisition and beneficial capital improvement of the property.

**5.3 Records**

The Valuer must keep a record of all facts, documents, notes and plans made, or relied upon, in the course of the inspection and valuation of the subject property. This record shall include the key inputs, all calculations, investigations and analyses relevant to the conclusion. These will form a permanent record of the work of the authorised Valuer for the Office of the Valuer-General. The records must be in a form that allows the Office of the Valuer-General to easily, independently and competently undertake a desktop review of the Valuer's work.

Relevant records include, but are not limited, to the following:

- Locality map of the subject property and comparable properties.
- Surveyor General diagram of subject property.
- Copy of title deed(s).
- Photographs of the subject property (preferably in colour)
- Videos of the subject property.
- Copies of all relevant documents, including field notes and sketch maps.
- Transcripts of interviews with owners, tenants or occupiers, as the case might be.

All records must be submitted to the Office of the Valuation-General, as addenda to the valuation report.

## 6. DETERMINING CURRENT USE VALUE

### 6.1 Principles

The first of the five factors that must be considered in the determination of value for the purposes of Section 12 of the Act is the 'current use of the property'. In operational terms, and in terms of the Regulations, this requires the authorised Valuer to determine the current use value of the property. The Regulations define current use value as "the net present value, as at the date of valuation, of cash inflows and outflows, or other benefits and costs that the subject property generates for the specific owner in perpetuity or, in the case of a lease, to lease expiry, under lawful use, and without regard to its highest and best use, or the monetary amount that might be realised upon its sale".

Current use value is to be treated as synonymous with the valuation concept 'use value' or 'value–in-use', with which it shares the above definition. Use value (value-in-use) derives from the utility obtained from the use of a property by a specific person. By contrast, market value derives from the utility as perceived by the broader market. Property may have a use value and a very different market value. For example, an old factory that is still used by the original firm may have a considerable use value to that firm, but only a nominal market value for another use. In this case use value may be higher than market value. In general, however, the use value of a property tends to be lower than its market value, because the former does not assume the highest and best use for the property.

In terms of International Valuation Standards (IVS), three categories of valuation bases are recognised. The second of these valuation bases, described as 'indicating benefits that a person or an entity enjoys from ownership of an asset' encapsulates use value. The IVS describes value derived in terms of this basis as 'specific to that person or entity and may have no relevance to market participants in general'. Defined like that, it is apparent that use value is close in meaning to investment value. The IVS in fact would regard the two as identical. The valuation basis and methods of determining both are the same. For the purposes of the work of the Office of the Valuer-General, however, the two must be distinguished from each other. Investment value should be taken to refer to value derived or perceived by a prospective purchaser of property, taking into account their specific needs, circumstances and capabilities. The difference between use value and investment value in this context, therefore, is that the former is from the perspective of a current owner while the latter is from the perspective of a prospective owner.

Current use value capitalises the benefits accruing to the owner of a property under a scheme of current use. It refers to the totality of benefits accruing to the owner arising from the combined employment of immovable, movable and intangible assets. An authorised Valuer should treat the subject property as a 'going concern', and should not, therefore, attempt to ascribe value to the physical real estate only.

To determine current use value, Valuers are required to compute the present value of the difference between cash inflows, or other benefits, and the present value of cash outflows, or other costs. This should be done using either the accounts (i.e. 'profits') or the income method of valuation. With respect to the income method, it is recommended that direct capitalisation (i.e. capitalisation one year's net income) rather than the Discounted Cash Flow (DCF) method be used. This is because the later requires more input variables, some of which are impossible to substantiate empirically, thereby complicating the valuation process and increasing the likelihood of errors. Further, the DCF approach is more ideally suited for the determination of investment value rather than use value.

The application of the profits and investment methods for the purposes of determining use value is, in principle, similar to when applied for the determination of market value, but with at least four critical differences.

**Firstly**, the Valuer must use actual benefits and costs accruing to or sustained by the owner of the subject property. Unlike in the determination of market value, Valuers are not to make the assumption of a 'reasonably efficient operator' 'or take into account 'potential', 'highest and best use' or 'market related' benefits and costs. The Valuer must take the benefits and costs accruing to the owner as they are, unless there are reasons to believe that there is material misrepresentation or fraud. This means a 'super-efficient' owner will have a higher use value whereas an inefficient one will have a lower value.

**Secondly**, unlike in the determination of market value, the determination of current use value require that the Valuer take into account as deductible expenses depreciation and amortisation charges. This is discussed in more detail in Section 6.3 below.

**Thirdly**, the definition of current value recognises that not all benefits and costs are captured by, or reflected in, cash flows. Examples include benefits (or avoided costs) arising from the occupation of own accommodation, or avoided costs associated with own or family labour. The Valuer must monetise these.

**Finally**, the capitalisation or discount rate used must be regarded as the opportunity cost of the property owner's capital, given their specific circumstances. These return measures, therefore, need not be 'market related', even as they may have to be constructed off a market base. The determination of market value, by contrast, requires the employment of market-derived rates of return.

### 6.2 Procedures

The practical procedure for the determination of current use value come in three slightly different versions, depending on whether the subject property is leased, or owner occupied and, with regard to the latter, whether reliable financial records exist or not. All three approaches will require a comprehensive analysis of revenues and expenditure, both actual and (for owner occupied property) imputed.

#### 6.2.1 Leased properties

The procedure to be followed by the Valuer in the case of leased property is relatively straightforward and involves the following steps:

- Research the income and expense data for the subject property (and as a check for possible misrepresentation and fraud) that of comparables.

- Estimate the potential gross income of the property by adding the rental income and any other income.
- Estimate the vacancy and collection loss.
- Subtract vacancy and collection loss from total potential gross income to arrive at the effective gross income of the subject property.
- Estimate the total operating expenses for the property. The treatment of expenses such as interest on loans and personal income taxes is explained in further detail in Section 6.3 below.
- Subtract the estimate of total expenses from the estimate of effective gross income to arrive at net operating income.
- Apply one of the capitalisation techniques to this data to generate an estimate of value. The direct capitalisation technique is to be preferred, but the 'hard-core and top slice' and the term and reversion' may also be used. It is generally not recommended to use the DCF method.
- The above procedure would be truncated in the case of a property leased on 'triple net terms' with the Valuer needing or to adjust the net income to take account into account relevant expenses and capitalising the adjusted net income in accordance with standard practice.
- In line with standard practice, the Valuer is to assume that expiring leases will be renewed at market rent, unless there is agreement to the contrary, or confirmation of non-renewal. Similarly, the Valuer is to assume that any vacancies (in excess of the natural vacancy rates) are to be leased at market rent, having due regard to the state of the market and making due allowances for anticipated letting delays.

6.2.2 Owner occupied properties – financial records present

The valuation of owner-occupied properties will require the Valuer to establish revenues and costs associated with the properties by means other than from lease agreements. This would be relatively easy in cases where the owner of the subject property keeps a complete set of financial records, especially if these are audited. These would form a more or less secure and reliable platform from which to construct the valuation cash flows. The general principle is that the Valuer will determine sustainable income expectancy for the subject property on the basis of the analysis of financial records. Owner-occupiers who run their properties as commercial businesses are required by law to keep financial records. Three financial records are key in this respect. These are the 'income statement' (i.e. 'profit and loss account', alternatively, the 'statement of financial performance'), the 'statement of financial position (i.e. the 'balance sheet'), and the 'cash flow statement'. The income statement shows the performance of the subject property over a defined period, and whether a profit or loss has been achieved, or incurred, respectively. The statement of financial position, on the other hand, displays, as at a specific date, all the assets (of the business on the property), including any profit or loss not distributed from previous accounting periods. The cash flow statement shows the movement of cash in and out of the subject property over a defined period, usually of one year.

In principle, either the 'profit and loss account' or the 'cash flow statement' could be used to determine the current use value. Profit is however not the same as cash, as the former is based on the accrual principle. That is to say, certain items of revenue or expenditure in the profit and loss account do not involve actual cash flows in the period for which they are reported. Thus, an entity may be profitable but may lack cash to pay suppliers (and be rendered insolvent). Conversely, an entity may show a positive cash flow but may inherently be unprofitable.

The ‘profit and loss account’ rather than the ‘cash flow statement’ should provide the basis for determining current use value. This is because profit is a better indicator of the long-term potential of the subject property and the sustainability of cash flows.

The procedure to be followed by the authorised Valuer where complete and reliable financial records exist is as follows:

- Obtain and analyse at least three years of the most recent financial statements.
- Establish from the balance sheet that the property is a going concern.
- The balance sheet of a going concern will show assets that exceed liabilities. The Valuer should in particular check that the current assets exceed the current liabilities. If this is not case, the entity may be insolvent and its profitability therefore not sustainable. The valuation considerations for cases of insolvency are detailed in a section below.
- Establish from the balance sheet that the subject property is the sole or most significant asset, and that the items of revenue and expenditure arise solely or mostly from the employment of this asset. This is to ensure that profitability can be attributed solely or mostly to the subject property. The valuation considerations for cases where the subject property is not the sole or most significant asset are detailed in a section below.
- From an analysis of the profit and loss account derive a projected annual sustainable income and expenditure statement. To be included as expenditure are depreciation and amortisation charges but not remuneration paid to them (see section 6.3 below for more detail).
- If not part of above, include the revenues and costs associated with movable assets that are normally and continually on the subject property, and which directly require the immovable property for their employment or use. Examples include cash flows arising from the keeping and sale of livestock.
- Add the imputed wages of unpaid own or family labour to the sustainable income, as well as the savings in accommodation costs due to occupation of own accommodation.
- From the projected sustainable income and expenditure statement derive the sustainable profit, i.e. annual earnings after depreciation and other allowable expenses.
- Capitalise the sustainable profit using an appropriate capitalisation rate. The process for selecting this rate is discussed in a section 6.4 below.

6.2.3 Owner occupied properties – no financial records

The general principles to be followed in circumstances where financial records are absent are similar to those where they exist, except that the valuer must establish sustainable annual income and expenditure expectancy, actual and imputed, by other means. The primary source for this information will be the owner, tenant or occupier of the subject property, who are legally required to provide it to authorised valuers. The valuer must however ensure that the information is accurate and reasonable. He or she must request to see proof of income and expenditure, by way of receipts and invoices. If these are not available, the valuer must proceed on the basis of what, on the basis of experience of comparable circumstances is reasonable. In determining the current use value of an owner-occupied property for which no financial records exist, the valuer must have regard to two key considerations.

**First**, the income and expenditure (or other benefits and costs) accruing to the owner must derive directly from the subject property. This is critical in cases where a property is being used as a base for a business that could, in principle, be carried out from another location. Without a process of attribution of the income and expenditure to the subject property, the current use value would be overstated.

The **second** key consideration is that the valuer must impute the benefit accruing to the owner for occupying own accommodation without payment of rent, and record this as income.

**6.3 Interest, depreciation and amortisation charges, and personal taxes**

The general valuation principle is that, if the objective is to determine market value, interest, depreciation and amortisation charges, and personal taxes are added back to income i.e. they are not treated as deductible expenses for the purpose of arriving at a sustainable profit expectancy. If the objective, however, it to determine current use value, as defined in the Regulations, these expenses are to be treated as follows:

6.3.1 Interest charges

Interest payments on loans secured on the subject property are not a deductible expense for the determination of market value because they are not an operational expense of the property. Interest payments are an outcome of discretionary funding decisions of the owners. Indeed, it may be the case that the proceeds of the loan are applied for purposes completely unrelated with the subject property.

The default position for dealing with interest costs for the determination of current use value is the same, namely, that interest costs should be added back to the income. In exceptional cases where the subject property is to be acquired together with all the loan liabilities of the owner, interest costs must be deducted as an expense.

The determination of current use value requires that actual costs (and benefits) accruing to the owner be taken into account. Interest charges represent a real cost and must therefore be taken into account. Failing to take them into account in circumstances where their loan liabilities have been taken over would put the property owner in a better position than they are in practice.

Unlike other costs associated with property, however, interest charges have a definite life span, in line with the term of the underlying loan. This means that it would be inappropriate to make a perpetual interest charge on the sustainable income of the property.

The correct treatment of interest cost in these exceptional circumstances is therefore, to determine the outstanding loan balance as a capital sum at the date of valuation, rather than take it as an annual cost.

6.3.2 Depreciation and amortisation charges

Depreciation and amortisation, as used in financial statements, represent the costs of assets, pro-rated over the lives of those assets. The difference between the two is that depreciation is used for tangible assets, such as immovable property, while amortisation is with respect to intangible assets, such as goodwill.

Accountants use the concept of depreciation (and amortisation) differently from the way it is conventionally understood by valuers. In accounting, it is a device by which the cost of an asset is related to the periodic incomes generated by that asset, as every income must be associated with a cost. Depreciation (and amortisation) is thus the periodic 'consumption' of original cost for the period during which the asset is in economic use. In terms of valuation theory, on the other hand, depreciation is a loss in the value of property arising from three things, namely, physical deterioration, functional obsolescence and economic obsolescence. These differences in conceptions between accountants and valuers notwithstanding, the basic underlying principle is similar. Depreciation (an amortisation) arises from the recognition that assets tend to lose value with time, and that renewal, or maintenance, is an inescapable requirement for their ownership.

Just like interest payments, depreciation and amortisation charges are not a deductible expense for the determination of market value because they are not operational expenses of the property. The added complication is that they are difficult to determine with a reasonable degree of accuracy and may be manipulated for tax avoidance reasons, making it difficult to make them directly comparable across different financial statements.

Depreciation and amortisation, however, represent a real cost of asset ownership, and must therefore be taken into account in the determination of current use value. In the case of leased properties, the valuer must make sure that there has been provision for maintenance in the operational costs of the property, and that this is reasonably adequate, given the nature of the property. While not exactly the same, maintenance costs could be taken as a proxy for depreciation. Where the subject property is owner-occupied, and audited financial statements exist, the valuer may use the depreciation charges reflected in the accounts. Where the subject property is owner-occupied, and no audited financial statements exists, the valuer must establish, primarily from the owner, the reasonable costs of maintenance.

6.3.3 Personal income taxes

Personal income taxes of the owner of the subject property are not a deductible expense for the determination of market value because they are not an operational expense of the property. Also, the level of taxes does not depend entirely on the income generated by the property, but on the owner's tax threshold, which depends on all their other incomes. There cannot, therefore, be a typical or standard property-related income tax expense. Personal income taxes are a personal liability for the owner of the subject property and are unlikely to be extinguished or transferred with the subject property. The correct treatment of income taxes is to add them back to the income.

**6.4 Capitalisation and discount rate selection**

The valuer must select a capitalisation rate or discount rate appropriate to the circumstances of the owner and of the subject property. Since the objective is to determine current use value, and not market value, the rate selected must reflect the required, achievable or appropriate rate of return for the owner, rather than that of the broader market. For practical reasons, however, the valuer should start with market rates of return, and adjust these to the specific circumstances of the owner and the subject property, on the basis of objective evidence and criteria. That is to say, the valuer should default to market rates unless there is objective evidence to the contrary, that the owner's cost of capital or required rate of return is, or should be, different from that of the broader market.

As stated above, the DCF method is not generally recommended for the determination of current use value. It is therefore expected that the task of rate selection would mostly involve determining a capitalisation rate, and not a discount rate. It is however easy to determine one from knowledge of the other, because the general relationship is that:

*Discount rate = capitalisation rate + inflation (projected growth in rental incomes and capital values)*

It is important to note that this relationship generally holds, but only if inflation in capital values is expected to be the same as that of rental values. There may be circumstances where this is not the case, where rental values change at a different rate from property prices. Under these circumstances, the valuer should not derive a discount rate from a capitalisation rate, or vice versa.

The valuer should generally, as far as possible, establish their own logically defensible rate and should not rely on third party providers. The main alternatives (to third party sources) are as follows:

6.4.1 Derivation from comparable sales

Under this approach, recent sales of properties similar to the subject property are analysed to arrive at the initial yield, which should then be adjusted to reflect the capitalisation rate appropriate to the owner and the subject property. The initial yield is the net income being achieved from the property at the date of sale divided by the price achieved. It is important to keep in mind that the initial yield is equal to the capitalization only if the property was leased at full market rental.

Derivation from comparable sales is the most valid approach to the determination of cap rates, but it is only possible if there are recent sales of similar properties. If these are not available, the valuer must use one the following alternatives.

6.4.2 Build-up method

Capitalisation rates represent rates of return required and/or achievable for property with a specific return-risk profile. These rates of return are comparable with other asset categories, with the relative differences in risk accounted for by differences in required or achieved returns. These alternative asset categories, especially government bonds, provide a basis from which capitalisation rates can be constructed. Conventionally, a capitalisation rate can be built from the bond rate according to the following formula (the risk premium being compensation for the additional risk of property over government bonds):

*Capitalisation rate = long bond rate + risk premium*

The challenge will lie in estimating the magnitude of the risk premium. There are no rules that can be prescribed on how this should be done, and the valuer must rely on experience and prevailing industry practice.

6.4.3 Alternative investment approach

The alternative investment approach is a variant of the build-up method. The difference is that the starting point for the construction of the capitalisation (or discount) rate is any alternative investment, rather than government bonds. A good base is commercial mortgages. From the perspective of the lender, mortgages are investments, with the interest rates charged being the required rate of return, given the risks associated with lending to particular individuals, property types or economic sectors. Interest rates are, in essence, the discount rates required by lenders in exchange for risks associated with providing credit. Since lenders have a prior claim to income produced by mortgaged property, it follows that the risk faced by property owners (hence their required return) is higher than that of lenders. This relationship allows the construction of a discount rate for property as follows:

*Discount rate = commercial lending rate + risk premium*

In practice, the valuer would need to establish average lending rates in, say, the agricultural sector or for property types similar to the subject property, and add a risk premium in order to determine an appropriate discount rate. The capitalisation rate can then be deduced from the discount rate by subtracting expected inflation, in terms of the relationship discussed above. Just like in the build-up method, the estimation of risk premiums presents a practical challenge.

6.4.4 Weighted-average cost of capital

Most property investments are financed by a mixture of equity and debt finance. Each of these will have different ‘costs’ to the investor. The weighted-average cost of capital (WACC) represents the weighted average cost of capital used by an investor. Investors in property frequently use their cost of capital as a target rate of return when appraising investment opportunities. It follows therefore, that if the valuer is able to determine the WACC of the owner of the subject property, that will provide a legitimate basis for deciding on an appropriate capitalisation rate to apply to that owner’s cashflows or other benefits. The valuer must however remain cognisant of the fact that WACC is used mostly for acquisition decisions, and therefore most appropriate for the determination of investment value. It should only be used for current use valuations if it is the only, or best evidence, of a return measure available.

**6.5 Dealing with special circumstances**

There will be circumstances where the capitalisation of existing cash flows or other benefits accruing to the owner and arising from the subject property may not provide the correct current use value or result in a negative value. Examples of the former include where there has been recent capital expenditure and where the consolidated cash flows can be attributed to multiple assets. The later will arise in circumstances where the cash inflows, or other benefits are less than the cash outflows, or other costs. In this case, the property owner may technically be insolvent, and possibly facing bankruptcy.

6.5.1 Factoring in major capital expenditure

Where the property owner, at the date of valuation, has just made a capital expenditure on the property whose effects are still to reflect in the cash flows or financial records, the capitalisation of these cash flows will generate an inaccurate current use value. The valuer must account for the unrealised impact of such capital expenditure. This requires that the actual cash flows be adjusted to reflect the effect of this expenditure, and with due regard to any timing delays. This adjustment must be reasonable and be based on objective factors, supported ideally by comparative market evidence.

6.5.2 Cases where the subject property is not the significant or sole asset

In cases where the subject property is not the significant or sole asset generating cash flows for the owner, capitalisation of these cash flows without adjustment will result in overvaluation of the owner's interest in the subject property. An example is where, for example, a printing business is located within a farm. In such a case, part of the consolidated cash flows will arise from the employment of the printing press, while part will arise from employment of the farm as an immovable asset. In theory, the printing business could be carried on from another site. Its valuation may in fact not form part of the valuer's instructions, or if it does, may need to be valued separately from the immovable property. Another example is where the accounts, relating to separate, or separable entities, or assets, have been consolidated.

The valuer must in such cases attribute a proportion of the cash flows to the subject (immovable) property and to such immovable property that are integral to the operation of the subject property. This can be done in one of two ways. In the one approach, if the valuer is able to attribute a proportion of the cash flows directly to the subject property, this should be done, and the valuation concluded as per procedure outlined above. If attribution of cash flows in this manner is not possible, the valuer must capitalise the entire cash flow and attribute part of the resultant value to the subject property pro rata on the basis of the relative market values of the assets contributing to the cash flow. It is recommended that the relative market values of the assets be established on the basis of comparable market evidence. If this is not possible, the book values of the assets in the balance sheet may be used to establish relative value.

The valuer must, however, keep in mind that the definition of current use value does not make a distinction cash flows, or other benefits, generated by immovable and movable property. It is the present value, to the owner, of the cash flows, and other benefits, arising from the employment of all assets on the subject property, arising from the ownership of the subject property. Thus there will be no need to undertake an attribution exercise where the assets concerned are inherently and naturally part of the subject property, and could not conceivably be separated from the ownership or operation of that property.

6.5.3 Dealing with insolvency

The definition of current use value generally assumes that the net present value cash of cash inflows, or other benefits, and cash flow outflows, or other costs, is positive. That is, the basic assumption is that inflows or benefits exceed outflows or costs. There, however, may be cases where this does not hold, and where, prima facie, costs exceed benefits. Such circumstances require the valuer to examine reasons for this state of affairs with particular care.

Reasons for insolvency are likely to lie in factors external to operational activities on the property itself. For example, financial stress may be caused by high interest payments on a mortgage secured on the property, but whose funds were applied elsewhere. A key characteristic of such reasons for insolvency is that the cash flows associated with them are not an inherent operational feature of the subject property is somewhat discretionary and are likely to be time limited in duration. Current use value is predicated on a sustainable, long-term view of cash flows accruing to the owner. The correct approach for dealing with time-limited factors causing insolvency is as laid out for interest charges above. That is to say, the valuer must compute whatever obligations are causing insolvency as a capital amount as at the date of valuation. As indicated above, how his capital sum is dealt with will depend on the circumstances of the acquisition of the subject property. If the acquiring authority is going to assume the financial obligations of the owner on the subject property, this capital sum must be deducted from the final current use value. If, on the other hand, the acquiring authority is not going to assume the any obligations, the capital sum must not be deducted.

If, however, after careful consideration, and having factored in the imputed benefits of occupation of own accommodation and own labour, the valuer finds that the cash flows are negative in a sustainable sense, the current use value must be recorded as nought, and not negative.

6.5.4 Dealing with timber and mineral property

In establishing the current use value, the authorised shall take into account the following:

- In the case of timber on the subject property, the full optimal rotation
- period for the tree species concerned; and
- In the case of mining property, imputed cashflows arising from mineral
- stockpiles and residual stockpiles on the subject property.

**6.6 Standards and/or guidance notes**

The determination of current use value requires a range of skills in addition to the standard competences in valuation methods, especially the application of the income and accounts methods. A critical skill in this regard is the ability to interpret and analyse financial statements, and to derive sustainable income expectancy from this analysis. This ability to understand and interpret financial statements, in turn, requires that the valuer develop a working knowledge of International Accounting Standards (IAS). These standards regulate how financial statements are prepared and presented.

There are no South African valuation standards or guidance notes dealing with current use valuations. No international standards are directly relevant as well. However, in terms of International Valuation Standards, the standard IVS 200 “Businesses and Business Interests” provides very useful guidance on the valuation businesses as ‘going concerns. As indicated above, the subject property should be regarded as a going concern for the purposes of determining current use value.

With respect to the standards of the RICS, the best general guidance is provided by RICS guidance note GN 2 “Valuation of individual trade related properties”. This guidance note deals with the valuation of property where the accounts method is indicated. It is a useful source of guidance on general principles for practical applications of this method. Valuers must, however, be aware that this guidance notice is meant for market valuations, and must therefore, make necessary adjustments for application to current use valuations, as described above.

## 7. FACTORING IN THE HISTORY OF ACQUISITION AND USE OF THE PROPERTY

### 7.1 Principles

The second of the five factors to be considered in the determination of value in terms of Section 12 of the Property Valuation Act is 'the history of the acquisition and use of the property'. This factor stems from the recognition of historical injustices associated with land dispossession, both under apartheid and in periods before. Numerous cases exist where the apartheid State, for example, expropriated property and sold it at well below market value. In these circumstances, beneficiaries of these expropriations, some of whom are current landowners obtained significant economic benefits from the State. It is generally accepted that the intention of the Constitution is that this benefit should be discounted from compensation to be paid. The rationale for this is that if such property was to be acquired from such owners now, it would be unfair to offer full market value as compensation because that will allow them to benefit twice from the state (Du Plessis, 2009).

Conceptually, applying this factor requires that the valuer to determine the value, as at the valuation date, of any acquisition benefits. The Regulations define "acquisition benefits" as any benefits that accrued to the owner of the property because of the manner of acquisition, and where such benefits did not arise from normal market transactions, including that they did not acquire the property on the open market from a willing seller.

### 7.2 Procedures

The acquisition benefits should be determined as follows:

- The facts and circumstances of the acquisition by the current owner
- should be recorded.
- The market value of the subject property at the time of acquisition by the
- current owner should be determined from an analysis of historical market
- information.
- The actual price paid by the current owner should be established. The
- difference between the historical market value and the actual price paid
- represent the historical acquisition benefits enjoyed by the current
- property owner.
- The value of these benefits should be determined as at the date of
- valuation in one of two ways.
- In the first approach, the historical acquisition benefit as a lump sum
- should be inflated at an appropriate index to the date of valuation.
- In the alternative approach, the proportion of the historical benefit to
- historical market value should be applied to the market value obtaining
- at the date of valuation in accordance with the following formula:

**(B-A)/B X C**

Where

**A** = the price the current owner paid originally;

**B** = the actual market value at the time of the original purchase

(and **B - A** is thus the historical acquisition benefit);

**C** = the current market value (i.e. market value as at the date of valuation), without the improvements which the current owner has added.

It is important to note that the alternative approach requires the valuer to discount the contribution to market value, as at the date of valuation, of improvements made by the current owner subsequent to acquisition, before applying the benefit proportion.

### 7.3 Valuation standards and/or guidance notes

In order to be able to apply the history of the acquisition and use of the property in the determination of value, valuers need to be able to undertake 'historical valuations' and to determine their present value. No standards on historical valuations in South Africa exist at the moment. The principles of doing these valuations are, however, exactly the same as those under which contemporary valuations are done, with time as the only key differentiator. Valuers will, therefore, be required to be competent in techniques for dealing with time series data, and in the construction and interpretation of price and cost indices. Section 9.4 below offers some guidance on how indices may be used to compute present day equivalents of historical amounts.

## 8. DETERMINING MARKET VALUE

### 8.1 Principles

The third of the five factors that the valuer needs to take account of in the determination of value in terms of Section 12 of the Property Valuation Act is the ''market value'' of the subject property. The Act defines market value as the estimated amount for which the property should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion, provided that in determining market value, prices paid by the State for any acquisition of property must be excluded. The Act further provides that in the event that no other credible data is available, prices paid by the State for any acquisition of property may be considered.

This definition of market value is broadly consistent with international definitions, including that provided in the International Valuation Standards, notwithstanding the different wording, and the exclusion of transactions for which the State is a party to. Standard definitions of market value generally discount the effects of 'special purchasers' i.e. purchasers who are atypical of the market and whose attitudes and behaviour would not reflect that of 'average' or 'normal' market participants. The reason is that prices paid by special purchasers could not provide a reliable guide to a property's likely selling price in the broader market.

In the South African context, prices paid by the State for property acquisitions could not be regarded as evidence for market value because the State is a special buyer for a number of reasons. First, the State cannot be conceived as a willing buyer envisaged in the definition of market value. Rather, the State is compelled by the constitution, legislation and a political-moral imperative to enter the market and acquire land for land reform. Second, consistent with the description of a special buyer, the State uses taxpayers' funds to purchase property acquired from the fiscus on terms ordinarily not available to private citizens. These funds are spent by civil servants who have no personal financial stake in the transactions they authorise and who, as a result, may be inclined to be over-generous or less diligent in their assessment of value for money. It is clear that the State cannot be placed on a similar footing with private citizens when it comes to market behaviour. Finally, the State does not necessarily have the luxury of unlimited time in which to conclude negotiations. Pressures arising from the budgetary cycle and from the need to meet targets means that transactions may be needing to be consummated in relatively short time periods, creating incentives for higher offer prices.

The Regulations to the Property Valuation Act imply that the determination of market value for compensation purposes is subject to the 'Point Gourde' principle. Named after a British Commonwealth court case (i.e., Pointe Gourde Quarrying and Transport Company Ltd v Sub-Intendent of Crown Lands 1947) this principle is a key component of land compensation law (Cristiano, 2009). It arises from the recognition that the involvement of government in undertaking a public project will often have a significant impact on property values in the vicinity of the area, which potentially could affect compensation payable (ibid.).

The Point Gourde principle requires that property that is subject to expropriation should be valued on the basis of the hypothetical highest and best use that it would have had had it not been needed for the public purpose for which it was acquired (ibid). The principle therefore requires that any increase or decrease in the value of the property arising from the carrying out, or the proposal to carry out, the purpose for which the property is being acquired should be disregarded in the determination of market value. This principle is embodied in the new Expropriation Bill/Act.

**8.2 Procedures**

It is expected that the authorised valuer will have the necessary competence to determine market value. This includes deciding on the appropriate method to use in each specific circumstance. The broad guidelines that follow, therefore, are not meant to be prescriptive, but rather to be suggestive of good practice.

They do not absolve the valuer of their responsibility to make appropriate professional judgements. The valuation procedures to be adopted will depend on the method selected, which in turn will depend on the nature of the subject property, and the objective market circumstances within which it is found. In general, market value should be determined by the sales comparison method, as it is the most persuasive and valid indicator of the most likely selling price. There will be circumstances however, where the use of the method is neither appropriate nor possible.

The general principles that should be followed in the determination of market value are as follows:

- Where there are sufficient sales and the properties are fairly homogenous, the sales comparison method should be used.
- Where the land value forms an overwhelming proportion of total value, such as in large farms, the depreciated replacement cost method should be used. That is to say, the land value should be determined using the sales comparison method and the value of the improvements determined using the depreciated replacement cost.
- Where the nature of the subject property is such that it is desired usually, or mostly, as an income-producing investment, the income method should be used. Such properties are likely to be leased. Section 8.3 below elaborates on the valuation considerations for this method.
- Where the nature of the subject property is such that it is desired usually, or mostly, as an income-producing investment, but where there is a limited market activity, the accounts or profits method should be used. Section 8.4 below elaborates on the valuation considerations for this method.
- Where the subject property is not at its highest and best use, and is desired for its development or redevelopment potential, the residual method should be used. Due to the sensitivity of the final valuation to input assumptions, and the difficulty of accurately establishing these, the residual method should only be used in exceptional circumstances, and where there are clearly no better alternatives.
- The cost method should generally be used as a method of last resort. It may be indicated in circumstances where there is no market evidence whatsoever, where the State is the only the player in the market, were land value forms an overwhelming proportion of total value, or in cases of brand-new speculative developments.

**8.3 Determining market value using the income method**

As suggested above, the income method should not be used as a first resort for the determination of market value. If circumstances warrant the use of this method, it is recommended that direct capitalisation, rather than discounted cash flow be used. The basic techniques and procedures are similar to those for determining current use value, as described in section 6.2 above. There are, however, and as indicated in that section, critical differences. The fundamental difference between current use value and market value is that whereas the former is value to the current owner, the latter is value in the broader market.

Market valuations require the valuer to assume that the property is being used at its highest and best use, and to factor in unrealised but realisable potential. The sales comparison method automatically takes these considerations into account, because comparable sales include potential, to the extent that that potential is perceived in the market.

In order that the income method leads the valuer to market value, he or she must ensure that all incomes and expenses must be market related. In line with standard practice for market valuations, the operating assumption must be that the property is, or could be, at its highest and best use. Thus, the subject property's incomes and expenditure might require adjustment to market, to reflect potential and highest and best use. Similarly, the capitalisation or discount rates used must be derived from the market.

8.3.1 Leased properties

The procedure to be followed in the case of leased property is relatively straightforward and involves the following steps:

- Research the income and expense data for the subject property (and as a check for possible misrepresentation and fraud) and that of comparables.
- Ensure that the income and expense data is market related, by making appropriate adjustments if necessary.
- Estimate the potential gross income of the property by adding the rental income and any other income.
- Estimate the vacancy and collection loss.
- Subtract vacancy and collection loss from total potential gross income to arrive at the effective gross income of the subject property.
- Estimate the total operating expenses for the property.
- Subtract the estimate of total operating expenses from the estimate of effective gross income to arrive at net operating income.
- Ensure that the net operating income is market related, by
- Applying one of the capitalisation techniques to this data to generate an estimate of value. The direct capitalisation technique is to be preferred, but the 'hard-core and top slice' and the term and reversion' may also be used. It is generally not recommended to use the DCF method.
- The above procedure would be truncated in the case of a property leased on 'triple net terms' with the valuer directly capitalising the net income in accordance with standard practice.
- In line with standard practice, valuers are to assume that expiring leases will be renewed at market rent, unless there is agreement to the contrary, or confirmation of non-renewal. Similarly, valuers are to assume that any vacancies are to be leased at market rent, having due regard to the state of the market and making due allowances for anticipated letting delays.
- Finally, only operational expenses of the property are to be deducted from the gross income of the property. Thus, interest charges, depreciation and amortisation, and personal income taxes of the owner must be ignored (or added back to the income).

8.3.2 Owner occupied properties

To determine the market value of an owner-occupied property using the income method will require the valuer to establish, from comparable market evidence, the market rental of the subject property, and to capitalise this using a market derived capitalisation rate.

### 8.4 Determining market value using the accounts method

As stated above, the accounts method is appropriate for the determination of the market value of 'business properties' that, due to factual circumstances or legal reasons have elements of being monopolies. The nature of markets for such properties is that there is no widely available evidence for establishing market rents and rates of return, thus making the use of the income method difficult.

The procedures for determining market value using the accounts method is, in principle, similar to that for determining current use value, and as described in section 6.2 above. There are, however, a couple of fundamental differences that the valuer must be cognisant of. These have been pointed out before. In addition to taking into account 'potential' and 'highest and best use', there are three specific considerations for determining market value on the basis of financial statements.

**First**, the valuer must assume a 'reasonably efficient operator' (REO). A reasonably efficient operator is one who is neither superefficient nor grossly inefficient. The valuer is thus required not to accept the financial statements as they are, but to test them for reasonableness in terms of the REO standard. This might require that the accounts be adjusted to bring them into line. The raison d'etre is that market value reflects the perspectives and capabilities of 'average' participants in the market, rather than that of 'outliers'.

The **second** consideration is that in the determination of market value from the accounts, only expenses arising from operational decisions regarding the subject property should be taken into account. Expenses arising from financing and accounting decisions must be disregarded (or added back to the income) before arriving at the 'divisible balance'. Thus, interest charges (being an artefact of financing decisions), and depreciation and amortisation charges (arising from accounting decisions) are to be added back to the income. Personal income taxes are not operational expenses of property and are to be treated in a similar fashion.

The **final** consideration is that the valuer must use a market-related discount or capitalisation rate to convert either the EBITDA (i.e. the 'divisible balance') or alternatively, the rental bid, into a capital sum as at the date of valuation. Capitalising the EBIDTA essentially leads the valuer to the total value of the property, to include both movable and immovable property, as both these contribute to total profit. That is, it leads to business value, rather than the value of the immovable property per se. In circumstances where there is a tight fit between the two, where the business is the subject property, capitalisation of EBIDTA is a legitimate approach to establishing market value.

Capitalisation of an appropriate 'rental bid' of the divisible balance, however, leads unambiguously to the market value of immovable property. For this reason, it is recommended that valuers use this approach, wherever possible. In the case of owner-occupied property, this approach requires the valuer to assume a hypothetical tenant as the operator, and to determine what proportion of net profit that they would be willing to pay as rent, with due regard to the nature of the business and market conditions. In order to fully reflect the costs faced by such a tenant, the valuer is required to work out the opportunity cost of the working capital required to operate the business. This cost may not be reflected in the financial statements.

Taking the above into consideration, the procedures to be followed by the valuer for determining market value using the accounts method are as follows:

- Obtain and analyse at least three years of the most recent financial statements.
- Establish from the balance sheet that the property is a going concern. The balance sheet of a going concern will show assets that exceed liabilities. The valuer should in particular check that the current assets exceed the current liabilities. If this is not case, the entity may be insolvent and its profitability therefore not sustainable. Using the accounts method to

determine market value requires that the property be a 'going concern'. If this is not the case, the valuer should not use the accounts method, but one of the alternatives.

- Establish from the balance sheet that the subject property is the sole or most significant asset, and that the items of revenue and expenditure arise solely or mostly from the employment of this asset. This is to ensure that profitability can be attributed solely or mostly to the subject property. Where the subject property is not the sole or most significant asset, the valuer must attribute the final value to the subject property in terms of the guidelines presented in section 6.5. Unlike for current use valuations, attribution is important in the case of determining market value because the regulations state that movable property should not be taken into account.
- From an analysis of the profit and loss accounts derive a projected annual sustainable income and expenditure statement, taking care to add back to the income non-operational and non-cash flow items, or items that arise purely from financing and accounting decisions (such as depreciation and amortisation charges, interest payments and personal taxes).
- From the projected sustainable income and expenditure statement derive the sustainable annual earnings before interest, depreciation and taxation (EBIDTA).
- If unavoidable, capitalise the EBIDTA using an appropriate capitalisation rate. In this case, the valuer must keep in mind the comments made regarding the relationship between EBIDTA and the value of immovable property.
- Alternatively (and this is the recommended approach), determine the average working capital required to run the business and deduct its opportunity cost from the EBIDTA. Also, to be deducted are any unavoidable costs that a hypothetical tenant has to incur in order to run the business.
- Apportion a proportion of the resultant figure as a rental bid, having regard to market practice or evidence.
- Capitalise the rental bid using a market-related capitalisation rate. The methods for determining discount and capitalisation rates have been described in Section 6.4 above. The valuer must bear in mind the different considerations in the employment of these rates between current use valuations and market valuations.

8.4.1 Owner occupied properties – no financial records

The valuer should not use the accounts method to determine the market value of an owner- occupied but for which no reliable financial records exist.

**8.5 Factors to exclude in the determination of market value**

The Regulations to the Property Valuation Act prescribe that the following factors should not be considered in the determination of market value:

- the fact that the property is the subject of an expropriation.
- the special suitability or usefulness of the property for which it is required by the acquiring authority, if it is unlikely that the property would have been purchased for that purpose in the opening market.

- any enhancement in the market value of the property, if such enhancement is a consequence of the use of the property in a manner which is unlawful.
- any diminution in the market value of the property, if such diminution is a consequence of being encumbered by a mining right, permit or permission, and where such encumbrance took place subsequent to assumption of ownership by the owner of the subject property;
- if the property is the subject of expropriation, improvements made on the subject property after the date on which the notice of expropriation was served, except where the improvements were in advance agreed to by the acquiring authority, or where they were undertaken in pursuance o obligations entered into before the date of expropriation.
- anything done with the object of obtaining compensation.
- if the property is the subject of expropriation, any enhancement or depreciation, before or after the date of service of the notice of expropriation, in the market value of the subject property, which can directly be attributed to the purpose in connection with which the property was expropriated.
- the value of any movable property, annual crops or growing timber on the subject property that have not yet been harvested as at the date of valuation, provided that the authorised valuer must determine their value separately if so requested by the instructing authority.

**8.6 Valuation of movable property**

In terms of the Regulations, movable property is to be valued separately, if so requested by the instructing authority. The basic approach is that if the movable assets in question have a clear market, and can be sold, the authorised valuer must value them at their net realizable value (NRV) as at the date of valuation.

As defined in this manual, NRV is the price of an asset that can be realised upon the sale of the asset, less a reasonable estimate of the costs associated with either the eventual sale or the disposal of the asset in question.

If the movable assets in question cannot be sold either because the assets are not separable, or have no market, the valuer must value them on the basis of depreciated replacement cost (DRC). As defined in this manual, the DRC is the cost of obtaining an alternative asset of equivalent utility; this can either be a modern equivalent providing the same functionality or the cost of reproducing an exact replica of the subject asset, less the accumulated depreciation of the subject asset.

**8.7 Valuation of growing crops**

Crops that have not been harvested as at the date of valuation, and that cannot be harvested and sold at that date, must be valued on the basis of total expenditure incurred on the crop up to that date.

**8.8 Valuation of growing timber**

The approach that should be taken in the valuation of timber depends on whether the timber has reached maturity, and can be harvested and sold, or is still immature. If the timber is mature, the valuer should determine its 'standing value'. In effect the standing value is the net realisable value of the timber crop as at the date of valuation. That is to say, the valuer must determine the gross sale value of the timber as the valuation date and subtract the cost of taking it to the market. These costs include felling costs and transport costs to the market, which might be a saw-mill.

If the timber is immature and has no immediate commercial value, the valuer should, in line with standard industry practice, use the Faustmann formula to determine its value.

**8.9 State transactions**

The default position is that prices paid by the state may not be used as evidence for market value. In terms of the Regulations, the valuer may depart from this injunction only

- He or she has taken reasonable steps to find comparable private transactions and finds that these are not available.
- Having regard to the facts and the circumstances of the transaction, and the broader property market, he or she believes, or should believe, that the price paid by the state is reasonable and fair and would represent what a private buyer would pay for the subject property, could one be found.
- He or she must disaggregate the total price paid by the state into prices paid for movable and immovable property, as appropriate, and report each component in accordance with the Regulations.
- He or she must flag and report his or her use of prices paid by the state as evidence for market value as a departure, as defined in the Regulations and in this manual.

**8.10 Standards and/or guidance notes**

The determination of market value involves a wide variety of circumstances and property types. There cannot, therefore, be a single and specific standard that provide general guidance. Due to the importance of the concept of market value to the valuation profession, the overwhelming proportion of valuation standards are related, in one way or the other, in providing guidance as to its measurement and reporting. Thus, the valuer is expected, and is in fact required as a professional obligation, to familiarise himself or herself with International Valuation Standards (IVS). The standards of the RICS (the ‘Red Book’) are highly recommended as being complementary to the IVS.

**9. FACTORING IN THE EXTENT OF DIRECT STATE INVESTMENT AND SUBSIDY**

**9.1 Principles**

The fourth factor that must be considered in the determination of value in terms of Section 12 of the Property Valuation Act is ‘the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property’. This subsection refers to circumstances where the acquisition by the owner of the subject property, and the capital improvement made to such property was made with the assistance of the (apartheid) state. The underlying rationale is that the current state should not compensate an owner for improvements that they made with apartheid state subsidies, as it will not be just and equitable to do so (Du Plessis, 2009).

The apartheid state made three specific kinds of investment and subsidies, namely, acquisition subsidies, in terms of which property was purchased from the state at below its true market value, interest rate subsidies arising from reduced interest loans that were made available for the acquisition of land, and infrastructure subsidies (mainly fencing subsidies) (DLA, 2000).

The Regulations to the Property Valuation Act prescribe that the authorised valuer shall determine the value, as at the valuation date, of any direct state investment and subsidy in the acquisition and beneficial capital improvement of the property accruing to the owner of the subject property. The Regulations state that where sufficient information exists, this value must be determined on the basis of current costs and prices depreciated to reflect value as at the valuation date. Where the relevant current information is lacking, the authorised valuer shall determine the historical value of state investments and subsidies and escalate the said value to the date of valuation using an appropriate cost or price index.

It must be stressed that, in the case of infrastructure, it is the contributory value of the subsidies to the subject property as at the valuation date that should be determined, and not the present-day equivalent of historical cost. To illustrate the point, the present-day equivalent of the cost of a subsidy that went into the construction of a borehole might be higher than the contributory value of that borehole if it is no longer in use currently. The valuer should, to the extent that this is possible, determine the value of the borehole to the current owner in its present state, and not simply escalate its historical cost.

**9.2 Procedures**

9.2.1 Acquisition subsidies

Procedures for determining the value, as the date of valuation dates, of acquisition subsidies is identical to that for determining acquisition benefits, as detailed in section 7.2 above. The difference between the two is that the latter are wider in scope than the former, and conceivably include acquisitions for which the State was not directly involved as enabler or facilitator. Because of the possibility that acquisition subsidies might overlap with acquisition benefits, authorised valuers must take care not to double-count these.

The procedure for determining the value of acquisition subsidies is as follows:

- The facts and circumstances of the acquisition subsidy by the current owner should be ascertained.
- The market value of the subject property at the time of acquisition by the current owner should be determined from an analysis of historical market information.
- The actual price paid by the current owner to the state should be established. The difference between the historical market value and the actual price paid represent the acquisition subsidy enjoyed by the current property owner at the time of acquisition.
- The value of these benefits should be determined as at the date of valuation in one of two ways.
- In the first approach, the historical acquisition benefit as a lump sum should be inflated at an appropriate index to the date of valuation.

- In the alternative approach, the proportion of the historical subsidy amount to historical market value should be applied to the market value obtained at the date of valuation in accordance with the following formula:

**(B-A)/B X C**

Where

**A** = the price the current owner paid originally

**B** = the actual market value at the time of the original purchase (And B- A is thus the historical subsidy amount)**;**

**C** = the current market value (i.e., market value as at the date of valuation), without the improvements which the current owner has added.

It is important to note that the alternative approach requires the valuer to discount the contribution to market value, as at the date of valuation, of improvements made by the current owner subsequent to acquisition, before applying the subsidy proportion.

9.2.2 Interest rate subsidies

The procedure for determining the value of interest rate subsidies is as follows:

- The amount that the owner of the subject property borrowed to purchase the property, as well as the loan term and interest rate should be determined. In the case of variable interest rates, the rates must be established for each year of the loan.
- The market interest rate at the time of the loan acquisition should be determined. If possible, the market rate should be determined for each year of the loan term.
- A loan amortisation schedule at the subsidised interest rate should be drawn, showing total loan repayments, capital repayments and interest repayments, per annum.
- Another loan amortisation schedule at the market interest should be drawn, showing what the owner of the property should have been paying by way of total loan repayments, capital repayments and interest repayments, per annum, had they borrowed at market rates.
- The difference, per annum, between interest payments at market rates and actual interest paid represents the interest rate subsidy per annum for the duration of the loan.
- The value of the series of annual interest rate subsidies as at the date valuation should be determined, by compounding each one to that date using a risk-free rate and adding the present values together. The long bond rate as at the date of the receipt of the interest rate should be used as the risk-free rate. This provides the most conservative result for the assumption that the interest rate subsidies were invested or were investable.

9.2.3 Infrastructure subsidies

These relate to the support provided by the State to landowners for the construction or acquisition of infrastructure, mostly boreholes, fencing and workers housing. The procedure for determining the value of infrastructure subsidies is as follows:

- The nature and type of infrastructure that was subsidised should be determined and described.
- The historical market cost of acquisition or construction of the infrastructure should be determined.
- The actual cost/price incurred/paid for the infrastructure by the current owner should be established. The difference between the historical market cost and the actual cost/price paid/incurred represent the infrastructure subsidy enjoyed by the current property owner at the time of acquisition.
- The value of these subsidies should be determined as at the date of valuation in one of two ways.
- In the first approach, the historical infrastructure subsidy as a lump sum should be inflated at an appropriate index to the date of valuation. For the reason mentioned above, this approach may, however, lead to inequitable results where the infrastructure in question no longer adds value as at the date of valuation, such as abandoned or disused boreholes.
- In the alternative (and recommended) approach, the proportion of the historical infrastructure subsidy amount to historical market cost of the infrastructure should be applied to the depreciated replacement cost of the infrastructure as at the date of valuation in accordance with the following formula:

**(B-A)/B X C**

Where

**A** = the cost/price the current owner incurred or paid for the infrastructure originally

**B** = the actual historical market cost of the infrastructure (and BA is thus the historical infrastructure subsidy amount)

**C** = the depreciated replacement cost of the infrastructure concerned as at the date of valuation, *pro-rated* to take into account any capital expenditure incurred by the owner on the infrastructure subsequent to the original acquisition.

**9.3 Determining the depreciated replacement cost of infrastructure**

The determination of the present value of infrastructure subsidies presents a number of difficult conceptual and technical challenges. The first approach, which is that of escalating the historical subsidy amount to the valuation date using a suitable index, has the advantage of simplicity, as long as the historical amount can be established. The problem is that, as has repeatedly been pointed out, cost is not value, and the present-day equivalent of historical cost might overstate the value of the infrastructure to the current owner. The **alternative approach,** that of using the depreciated replacement cost of the infrastructure as at the date of valuation has the advantage of providing a more equitable result but is much more complicated to apply in practice. This alternative is recommended, but works best, or easier, if the current owner has not made (major) capital expenditure on the subsidised infrastructure subsequent to the original acquisition.

The pro-rated depreciated replacement cost, for the purposes of the second alternative, (the C in the formula above) should be determined as follows:

- Identify the infrastructure on the subject property whose acquisition or construction was subsidised by the State.
- Estimate the total replacement cost of the infrastructure as at the valuation date.
- Estimate the amount of depreciation in the infrastructure as at the date of valuation.
- Deduct estimated depreciation from the total replacement cost of the infrastructure to derive an estimate of their depreciated replacement cost.
- Estimate the proportion of current replacement cost that can be attributed to the current owner having made capital expenditure on the infrastructure subsequent to the original acquisition, and deduct this from the depreciated replacement cost, to be left with a pro rata depreciated replacement cost (i.e., the C in the formula above).

**9.4 Chaining (or 'splicing') and applying index numbers**

The escalation of historical subsidy amounts (and acquisition benefits described in Section 7 above) to present-day equivalents require the valuer to apply appropriate cost or price indices. CPI should generally be used as the default measure to capture changing price levels, unless a more valid index is available, given the nature, or location, of the property in question. CPI data for the whole country is available for fairly long periods going into the past. The problem is that national CPI rates present a broad-brush view and may not be appropriate where there are significant regional differences in price inflation, or where the item in question has an inflation rate that is markedly different from CPI. For these reasons, the valuer must use CPI only if a regional or item -specific index is not available.

It is the norm for long running indices, like CPI, to be rebased to 100 from time to time. In order to be able to use indices with different bases, the valuer needs to 'chain' or 'splice' them together. The table below will be used to show how this is done, and how an index may be used to escalate a historical amount to an equivalent amount as at the date of valuation.

The table below shows two indices, A and B with different base years. To chain them together, the following steps should be carried out:

**Step 1** - Identify one period when there are figures for both indices (1992 in this case)

**Step 2** - For this period, divide the new figure by old figure (83 / 133 = 0.62)

**Step 3 -** Multiply all old figures by the result (each figure in column C = figure in column A * 0.62).

**Step 4** - Put the rebased data with the new figures to create one long run of data (column D).

**9.5 Standards and/or guidance notes**

In order to be able to apply the 'extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property' to the determination of value, valuers need to be able to undertake 'historical valuations' and to determine their present value. No standards on historical valuations in South Africa exist at the moment. In order to apply this factor, the valuer will need knowledge regarding the time value of money, and of the construction and interpretation of index numbers.

| | **Old Index** | **New index** | **Old Index Rebased** | **Chained index** |
|---|---|---|---|---|
| | **A** | **B** | **C** | **D** |
| 1989 | 100.0 | | 62.0 | 62.0 |
| 1990 | 110.0 | | 69.0 | 69.0 |
| 1991 | 121.0 | | 76.0 | 76.0 |
| 1992 | 133.0 | 83.0 | 83.0 | 83.0 |
| 1993 | | 91.0 | | 91.0 |
| 1994 | | 100.0 | | 100.0 |
| 1995 | | 110.0 | | 110.0 |

The chained index (column D) can now be used to estimate the equivalent value, at any date on the index, of a known historical amount in accordance with this formula:

**A/B X C**

Where

**A** = the index number at the date of valuation;

**B** = the index number at the date of the historical amount;

**C** = the historical amount.

To illustrate with an example, suppose a farm, with a market value of R1,000,000 was purchased in 1989 for R800,000, with the balance accounted for by an acquisition subsidy (of R200,000). The equivalent amount of the subsidy in 1995 can be calculated as follows:

110/62 X 200,000 = **R354 838. 71**

## 10. FACTORING IN THE PURPOSE OF ACQUISITION

### 10.1 Principles

The fifth and final factor to be taken into account in the determination of value in terms of Section 12 of the Property Valuation Act is “the purpose of acquisition”. There will be numerous specific purposes for which the State might

acquire private property. It is however neither practical, nor necessary, to list all of these conceivable purposes, let alone try to work out their valuation implications. Rather, all reasons will fall into one of only two categories – an acquisition that is for a ‘public purpose’ or one which is in the public interest. That is to say acquisition of property by the State by expropriation may for public purposes or ‘in the public interest.

Expropriation for public purposes is where property is acquired from a private individual for the benefit of the public more generally, such as for infrastructure development. This normally precludes expropriation from private individuals to directly benefit other identified private individuals. As such, expropriation for public purposes would not cover situations obtaining in land reform, where the beneficiaries are specific individuals. Expropriation in the public interest on the other hand is broader in scope and allows for the compulsory acquisition of property to benefit specific individuals, such as beneficiaries of land reform programmes. Indeed, section 25(4) of the constitution specifically describes the 'nation's commitment to land reform' as to be in the public interest. There is, therefore, no doubt whatsoever that the provisions of section 25(3) are directly relevant and applicable to the determination of compensation for property acquired in the context of the land reform programme.

### 10.2 Valuation implications

Valuers should interpret this factor as merely legitimising the application of section 25(3) and has no implication on the amount of compensation. The purpose of expropriation in circumstances envisaged by these guidelines is land reform. This is explicitly described in the constitution as being in the public interest, and therefore falling within the scope of application of section 25(3).

In practice, no discretion shall be given to authorised valuers regarding the purpose of acquisition, as this will be part of the instructions given to them. Authorised valuer shall merely, on the basis of instructions received from the instructing authority, attest that the purpose of acquisition of the subject property is either in the public interest or for a public purpose, as the case may be, and proceed to apply the other factors.

## 11. DETERMINING OVERALL VALUE IN TERMS OF THE PROPERTY VALUATION ACT

### 11.1 Integrating the factors

In terms of the Regulations to the Property Valuation Act, authorised valuers shall determine the value of the subject property for the purposes of section

12(1)(a) of the Property Valuation Act by:

(a) Where the immovable property is to be acquired together with movable property, annual crops or growing timber on the subject property that have not yet been harvested as at the date of valuation-

i. adding the current use value and market value of the subject property as at the date of valuation, and as established in terms of regulation 5, and dividing the resulting figure by two;
ii. subtracting from the resulting figure the value, as at the date of valuation, of acquisition benefits and the value of direct state investment and subsidy in the acquisition and beneficial capital improvement of the subject property; and
iii. provided that the value of movable property, annual crops or growing timber on the subject property that have not yet been harvested as at the date of valuation, and as established in terms of Regulation 5, must be added to market value before the division referred to in sub regulation (i) is performed.

(b) Where the immovable property is to be acquired without movable property, annual crops or growing timber on the subject property that have not yet been harvested as at the date of valuation-

i. adding the current use value and market value of the subject property as at the date of valuation, and as established in terms of regulation 5, and dividing the resulting figure by two;
ii. subtracting from the resulting figure the value, as at the date of valuation, of acquisition benefits and the value of direct state investment and subsidy in the acquisition and beneficial capital improvement of the subject property; and
iii. provided that the value of movable property, annual crops or growing timber on the subject property that have not yet been harvested as at the date of valuation, and as established in terms of Regulation 5, must be subtracted from current use value before the division referred to in sub-regulation (i) is performed.

**11.2 Other relevant factor**

A reading of Section 25 of the constitution suggests that the five factors listed therein are not exclusive, and that other relevant factors need to be taken into account in the determination of compensation. It is, however, not practical to identify all conceivable factors in advance, let alone work out their valuation.

The approach taken by the Office of the Valuer General is that if there any other factors that need to be considered; they will come to light in the process of the judicial process and dealt with by the Courts.

**12. VALUATION REPORTS**

**12.1 Format of valuation reports**

In terms of the Regulations, the following are the minimum contents for valuation reports to be submitted by authorised valuers:

- identification of the instructing authority and any other intended users;
- the purpose of the valuation;
- legal description of the subject property;
- whether the subject property is encumbered, the extent of the encumbrance and the financial institution(s) involved
- the interest that was valued;
- the valuation basis, or bases;
- the date (s) of inspection;
- the valuation date;
- disclosure of any material involvement in the subject property by the authorised valuer, or a statement that there has not been any previous material involvement;
- the identity of the valuer responsible for the valuation and, their registration status;
- any assumptions, special assumptions, reservations, special instructions or departures;
- the extent of the authorised valuer's investigations;
- the nature and source of information relied on by the authorised valuer;

- any consent to, or restrictions on, publication of the report;
- any limits or exclusion of liability to parties other than the instructing authority, or the Valuer-General, as the case may be;
- confirmation that the valuation accords with the provisions of the Act, Regulations and any other applicable prescripts;
- a statement regarding the purpose of acquisition;
- a statement of the valuation approach or approaches and reasoning;
- the current use value of the property;
- a statement regarding the history of the acquisition and the use of the subject property, and the historical and present values of any acquisition and use benefits accruing to owner;
- the market value of the property;
- a statement regarding the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property, and their historical and present values;
- a list of all movable properties on the subject property;
- the value of the subject property as at the valuation date; and
- a valuation certificates.

**12.2 Reporting standards and/or guidance notes**

There are no South African standards for valuation reporting. Subject to the Property Valuation Act, the Regulations and this manual, the format of valuation reports must conform to International Valuation Standards, namely IVS

OFFICE OF THE VALUER-GENERAL

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