

The Valuation of Business Property

GUIDANCE TO CUSTOMERS AND CONDITIONS OF ENGAGEMENT

What are valuations and appraisals?

A valuation is a professional individual's opinion of the capital or rental price or value of a property on a defined basis. It is founded upon relevant facts and defined assumptions.

An appraisal provides opinion, advice and/or analysis relating to the suitability or profitability of a property for the Client's purpose, in addition to a valuation.

Defining the service to be provided

In order to ensure that Clients get valuations or appraisals which meet their needs, it is essential that we know the purpose for which the service is required. This enables the most appropriate valuation basis to be adopted and the Report to cover the matters which are important to the Client.

For this reason, and to ensure that the Valuer has the appropriate knowledge, skills and understanding (in some cases these are regulatory requirements), we seek to establish the purpose of the particular valuation or appraisal. We will disclose any conflict of interest of which we are aware and agree and confirm your instructions in writing before issuing the Valuation Report.

Often a preliminary discussion with the Valuer will be of benefit so that potential areas of uncertainty can be resolved, the Client's needs understood and arrangements for assembly of the necessary information made.

A formal environmental assessment is not provided. It is necessary to agree whether the property is to be valued a) on the assumption that there is no contamination or b) that the valuation is to reflect the contents of an environmental audit, land quality statement or similar environmental report prepared by a specialist advisor or c) the arrangements to apply in respect of any appointment of consultants to investigate and report upon contamination and provide an estimate of remedial costs.

On occasion, however, it may be necessary to confirm/agree that the Valuer will make preliminary enquiries to enable a decision to be taken as to which of the arrangements outlined in the previous paragraph is to be adopted.

Usually the Report is confidential to the Client and our consent will be required before any part of the Report can be published or referred to publicly; our liability does not extend to third parties. It would be misleading if a valuation were relied upon by a person who knows neither the basis on which, nor the purpose for which, a valuation has been prepared. For instance, a valuation for a market purpose must never be confused with an assessment for insurance purposes. The latter is usually an estimate largely of the cost of rebuilding, the former a reflection of property transaction prices.

Valuation or survey?

It is important to appreciate that a valuation is not a building survey. The Valuer will have regard to apparent defects and wants of repair and will take into account the use and nature of the property. The Valuer will not, however, carry out the detailed search for defects which is undertaken as part of a building survey, nor necessarily report the various defects observed.

Similarly, it is extremely difficult to check whether potentially harmful or hazardous materials or techniques have been used in the construction of a building, or have been incorporated subsequently, without an investigation, possibly including chemical analysis, by a specialist surveyor or structural engineer.

Unless additional arrangements have been made, Clients should expect the Conditions of Engagement and Report to include caveats which record that these matters have not been investigated and have been assumed not to be material to the valuation. If the Client requires not just a valuation but also some form of survey, we can provide this, and/or arrange specialist investigations if the Client so wishes. Of course, such additional work and responsibility involves a higher fee.

The valuation bases

Unless it is specified by law or prescribed by a legal agreement, a valuation basis must be agreed between the Client and ourselves to reflect the purpose of the valuation.

There are a number of valuation bases which our Valuer must use in defined circumstances, unless there are justifiable reasons for departing from them or for making additional assumptions.

It is important that all parties are aware of, and understand, what these respective valuation bases provide.

Market Value (MV) is defined as:

The estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion:

'The estimated amount ...'

Refers to a price expressed in terms of money (normally in the local currency) payable for the property in an arm's-length market transaction. *Market Value* is measured as the most probable price reasonably obtainable in the market at the date of valuation in keeping with the *Market Value* definition. It is the best price reasonably obtainable by the seller and the most advantageous price reasonably obtainable by the buyer. This estimate specifically excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements, special considerations or concessions granted by anyone associated with the sale, or any element of Special Value. (d) that no account is taken of an additional bid by a prospective purchaser with a special interest, and



'... a property should exchange ...'

Refers to the fact that the value of a property is an estimated amount rather than a predetermined or actual sale price. It is the price at which the market expects a transaction that meets all other elements of the Market Value definition should be completed on the date of valuation.

'... on the date of valuation ...'

Requires that the estimated *Market Value* is time-specific as of a given date. Because markets and market conditions may change, the estimated value may be incorrect or inappropriate at another time. The valuation amount will reflect the actual market state and circumstances as of the effective valuation date, not as of either a past or future date. The definition also assumes simultaneous exchange and completion of the contract for sale without any variation in price that might otherwise be made.

'... between a willing buyer ...'

Refers to one who is motivated, but not compelled to buy. This buyer is neither over-eager nor determined to buy at any price. This buyer is also one who purchases in accordance with the realities of the current market and with current market expectations, rather than on an imaginary or hypothetical market which cannot be demonstrated or anticipated to exist. The assumed buyer would not pay a higher price than the market requires. The present property owner is included among those who constitute 'the market'. A valuer must not make unrealistic Assumptions about market conditions or assume a level of Market Value above that which is reasonably obtainable.

'... a willing seller ...'

Is neither an over-eager nor a forced seller prepared to sell at any price, nor one prepared to hold out for a price not considered reasonable in the current market. The willing seller is motivated to sell the property at market terms for the best price attainable in the (open) market after proper marketing, whatever that price may be. The factual circumstances of the actual property owner are not a part of this consideration because the 'willing seller' is a hypothetical owner.

'... in an arm's-length transaction ...'

Is one between parties who do not have a particular or special relationship (for example, parent and subsidiary companies or landlord and tenant) which may make the price level uncharacteristic of the market or inflated because of an element of *Special Value* (see IVS 2, paragraph 3.8). The *Market Value* transaction is presumed to be between unrelated parties each acting independently.

'... after proper marketing ...'

Means that the property would be exposed to the market in the most appropriate manner to effect its disposal at the best price reasonably obtainable in accordance with the *Market Value* definition. The length of exposure time may vary with market conditions, but must be sufficient to allow the property to be brought to the attention of an adequate number of potential purchasers. The exposure period occurs prior to the valuation date.

'... wherein the parties had each acted knowledgeably, prudently ...'

Presumes that both the willing buyer and the willing seller are reasonably informed about the nature and characteristics of the property, its actual and potential uses and the state of the market as of the date of valuation. Each is further presumed to act for self-interest with that knowledge and prudently to seek the best price for their respective positions in the transaction. Prudence is assessed by referring to the state of the market at the date of valuation, not with benefit of hindsight at some later date. It is not necessarily imprudent for a seller to sell property in a market with falling prices at a price which is lower than previous market levels. In such cases, as is true for other purchase and sale situations in markets with changing prices, the prudent buyer or seller will act in accordance with the best market information available at the time.

'... and without compulsion.'

Establishes that each party is motivated to undertake the transaction, but neither is forced or unduly coerced to complete it.

The valuations should include any development potential of which the market would take account.

Existing Use Value (EUV) follows the definition of MV but with the following two additional assumptions:

- the property can be used for the foreseeable future only for the existing use; and

- that vacant possession is provided on completion of the sale of all parts of the property occupied by the business (save that, solely where the property is owned by a public or other non profit-making body for the delivery of a service, it is to be assumed that the property will continue to be occupied or let for its existing use).

This is a basis for use only when valuing, for Clients' financial statements, property which is occupied for the purposes of their businesses. Another basis of valuation used in such circumstances is Depreciated Replacement Cost (DRC) - where it is not practicable to assess the EUV.

The valuation of certain classes of property, such as hotels, leisure and licensed property, private healthcare facilities and petrol filling stations, may be valued as fully operational entities having regard to trading potential.

There are equivalent valuation bases available, for rental values, and for when the period to be assumed for marketing and conveyancing is insufficient to allow the property to be fully exposed to the market.

A valuation may be required for many purposes including sale, purchase, letting, obtaining finance, accounting, rating, compulsory purchase and taxation. What appear as minor differences in the purpose for which a valuation is to be used (for example, one tax calculation rather than another) can lead to significantly different figures, clearly demonstrating the need to define the purpose of valuation.

The property to be valued may be freehold, leasehold or some other interest, such as an easement or a restrictive covenant, and may, itself, be subject to other interests. It is important to note that what appear to be relatively minor variations in lease terms, or small variations in planning conditions, can also affect value.

About the valuation service

The service provided and our Report will depend upon what has been agreed is to be provided, the extent of the inspection possible or permitted, the information provided or obtained and the time allowed in which to produce the Report.

Normally we will carry out an inspection of the premises and will make such enquiries and investigations as are deemed necessary. These may involve oral enquiries of the Local Planning Authority and other authorities. Although we may sometimes obtain written confirmation of details provided orally by such authorities, it will usually be necessary for the Client's Solicitor to make formal enquiries



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If the Client so requires, we will arrange or undertake further investigations to enable written advice or confirmation to be provided on matters arising. On occasions such investigations can lead to a revised opinion of value and additional costs.

It is possible that a Client may require a valuation based only on an external inspection, in which case the Valuer must rely on information provided in relation to floor space and other matters.

We will often have to rely upon information provided by the Client, the Client's Solicitor or Accountant as, for example, in the case of legal restrictions or tenancy agreements or whether the valuation is by reference to accounts. We will not take responsibility for the interpretation of legal documents. There will be instances where our Valuer will need to examine copies of appropriate documents, such as leases, and where these are not available the Report will refer to the assumptions made or the information which has been provided.

The RICS has laid down minimum standards of valuation reporting with which its members are required to comply.

What will it cost?

There are no national scale fees and the fee in each case will depend upon the nature and extent of the work. Kirkby and Diamond will provide quotations for specified valuations. In addition VAT is usually payable, and sometimes reasonable out-of-pocket expenses.

Conditions of Engagement

1. The purpose of the valuation shall be agreed between the Client and Kirkby and Diamond.
2. The subject, including treatment of fixtures, fittings, plant and machinery and tenure (freehold/leasehold) of the property to be valued shall be as specified by/agreed with the Client.
3. Unless otherwise agreed, the basis/bases of valuation to be provided will be as prescribed by The Royal Institution of Chartered Surveyors and agreed/confirmed in writing by Kirkby and Diamond to the Client before the Report is issued, together with any special assumptions relating to the basis/bases.
4. Subject to paragraphs 6 and 7 below, our Valuer shall carry out such inspections and investigations as are, in the Valuer's professional judgement, appropriate and possible in the particular circumstances.
5. We will rely upon information provided by the Client and/or Client's legal or other professional advisers relating to tenure, tenancies and other relevant matters.

6. We will have regard to the apparent state of repair and condition of the property but will not carry out a building survey nor inspect those parts of the property which are covered, unexposed or inaccessible. Such parts will be assumed to be in good repair and condition. The Valuer will not be under a duty to arrange for the testing of electrical, heating, plant or other services.

7. In reporting Kirkby and Diamond will meet the relevant requirements of the RICS Appraisal and Valuation Manual and will make the following assumptions, which we will be under no duty to verify:

(a) that no harmful or hazardous material has been used in the construction of the property or has since been incorporated, and that there is no contamination in or from the ground, and it is not landfilled ground;

(b) that good title can be shown and that the property is not subject to any unusual or especially onerous restrictions, encumbrances or outgoings;

(c) that the property and its value are unaffected by any matters which would be revealed by a local search and replies to the usual enquiries, or by any statutory notice, and that neither the property, nor its condition, nor its use, nor its intended use, is or will be unlawful;

(d) that inspection of those parts which have not been inspected would neither reveal material defects nor cause the Valuer to alter the valuation materially.

8. The Report will be provided for the stated purpose(s) and for the sole use of the named Client. It will be confidential to the Client and the Client's professional advisers. Kirkby and Diamond accepts responsibility to the Client alone that the Report will be prepared with the skill, care and diligence reasonably to be expected of a competent Chartered Surveyor, but accepts no responsibility whatsoever to any parties other than the Client. Any such parties rely upon the Report at their own risk. Neither the whole or any part of the Report nor any reference to it may be included in any published document, circular or statement nor published in any way without our written approval of the form and context in which it may appear.

9. The Client will pay Kirkby and Diamond the fee agreed/confirmed in writing by us and the amount of any Value Added Tax on the fee. In addition, if similarly agreed/confirmed in writing, the Client will reimburse Kirkby and Diamond the cost of all reasonable out-of-pocket expenses which may be incurred, and any VAT thereon.

Kirkby and Diamond operate a complaints procedure, details of which will be made available to the client on request.

