

The Valuation of Business Property: Guidance to Clients

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 the Valuer knows 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, the Valuer is required to seek to establish the purpose of the particular valuation or appraisal. The Valuer is obliged also to disclose any conflict of interest of which he is aware and to agree or confirm instructions in writing before issuing the Valuation Reports.

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 on the assumption that there is no contamination; or that the valuation is to reflect the contents of an environmental audit, land quality statement or similar environmental report prepared by a specialist adviser, and if so 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 the Valuer's consent will be required before any part of the Report can be published or referred to publicly, and the Valuer's 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 market purposes must never be confused with an assessment for insurance purposes. The latter is usually an estimate of the cost of rebuilding, the former a reflection of property transaction prices.

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Valuation or Survey?

It is very 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 their Valuers' Conditions of Engagement and Reports 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, the Valuer will be prepared to provide this and/or arrange specialist investigations if the Client so wishes. Of course, such additional work and responsibility involves a higher fee.

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The Valuation Bases:

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

The Practice Statements and Guidance Notes contained in the “RICS Valuation Standards, 6th edition” published by the Royal Institution of Chartered Surveyors (RICS) defines a number of valuation bases which the 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.”

Worth, or Investment Value is defined as:

“The value of property to a particular owner, investor, or class of investors for identified investment or operational objectives.”

Fair Value is defined as:

“The amount for which an asset could be exchanged, between knowledgeable, willing parties, in an arm’s length transaction.”

The valuation of certain classes of property, such as hotels, leisure and licensed property 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 of 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 and taxation. What appear as minor differences in the purpose for which a valuation is to be used, can lead to significantly different figures, clearly demonstrating the need to define the purpose of the valuation.

The property to be valued may be freehold, leasehold or some other interest, such as an easement 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.

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About the Valuation Service:

The service provided and the Valuer's 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 the Valuer 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 the Valuer may sometimes obtain written confirmation of details provided orally by such authorities it will usually be necessary for the Client's legal advisers to make formal enquiries.

If the Client so requires, the Valuer 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.

The Valuer will often have to rely upon information provided by the Client or the Client's legal adviser or accountant, as for example in the case of legal restrictions or tenancy agreements or whether the valuation is by reference to accounts. The Valuer will not take responsibility for the interpretation of legal documents. There will be instances where the Valuer will need to examine copies of appropriate documents, such as leases, and where there 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 scale fees and the fee in each case will depend upon the nature and extent of the work. The Valuer will provide quotations for specified valuation. In addition, VAT is usually payable and reasonable out of pocket expenses.