SUBMISSION TO

THE VALUER GENERAL

on the Draft Regulations in terms of The Property Valuations Act (Act 17 of 2014)

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1. Introduction to Forestry South Africa

Forestry South Africa (FSA) is an Association which represents the interests of its members in particular and the promotion and wellbeing of the South African commercial Forestry Industry in general. Although voluntary in its nature, FSA's membership includes all 11 corporate timber companies, including their subsidiaries, operating in South Africa, 1 100 commercial timber farmers and over 20 000 small-scale black timber growers. This membership represents over 90% of the Industry as a whole and virtually all the private sector involved in the Industry. Due to this representivity, FSA is viewed by both Government and the Private Sector as **the** body which represents the South African Forestry Industry.

FSA is involved in a host of areas such as research 123, education and training, water and environmental affairs, forest protection, bio-energy, business development and transport. We also involve ourselves in any regulations or legislation which may have an impact on our members' interest.

This submission, for which we are grateful of the opportunity to be able to make, is made on behalf of the South African Forestry Industry by Forestry South Africa.

2. Background to the South African Forestry Industry

The South African Forestry Industry is based on 1.2 million hectares of man-made plantations and is, by any measure, an important sector of the economy, employing 62 000 people directly, producing over R9.5bn worth of products annually and supporting a primary processing sector which employs a further 50 000 people directly, which produces value added products worth over R40bn. In 2016 exports of forest products totalled R29.1bn which earned the country net foreign exchange earnings of R9.3bn. In addition, the Industry is a major catalyst for rural development and has the potential to create an estimated 30 000 extra jobs in the country, particularly in Zululand and the Eastern Cape.

Other characteristics include the following:

- Ownership of the plantation resource can be split into four distinct categories, namely, Corporate timber companies (11), commercial timber farmers (1 300), small-scale timber growers (25 000) and the State. In terms of area, the following can be noted:

Category	Hectares	% to Total
Corporate Timber Companies	612 600	50.0%
Commercial Timber Growers	210 368	17.2%
Corporate Timber Companies (ex Safcol)	143 300	11.7%
Safcol (through Komatiland Forests)	127 700	10.4%
State	85 488	7.0%
Small-Scale Timber Growers	45 000	3.7%
Total	**1 224 456**	**100.0%**

- Between 16 and 17 million tons of timber is produced on a sustainable basis annually, all of which needs to be transported to the 144 processing plants which convert this roundwood into pulp and paper, sawn timber (lumber), poles, mining timber and other products such as woodchips, charcoal and matches.

- Investment in the South African Forestry Industry in 2015 was estimated at R42.7bn. This was broken down as follows:

Asset	**Value R/bn**	**% to Total**
Trees	R21.1	49.4%
Land	R15.8	36.9%
Roads	R3.4	8.0%
Fixed Assets	R1.8	4.2%
Moveable Assets	R0.6	1.5%
Total	**R42.7**	**100.0%**

  The market value of this investment is between 12% and 18% higher than this figure – i.e. between R47.8bn and R50.4bn. Of importance to note is that trees account for almost half of the total – much more than bare land.

- Valuation methodologies used in Industry for tree crops:
  - Standing values (CGT & selling of timber)
  - Replacement values (Faustmann)
  - NPV (business value)

  The valuation of forestry land is based on the “comparable sales” method.

- Average long-term return is around 5% but varies per crop, per year.

- Due to long rotation ages, cash flows are highly uneven and thus net profit is very volatile and can vary considerably between crops and per year. Net profits can frequently be negative.

- With regards land reform, the following is pertinent:
  - Estimated that +- 70% of forestry land is under claim
  - Land reform models have been developed by Industry to ensure sustainability
  - Where lease back used, rent paid to beneficiaries is based on land value
  - Very few restitution transfers have occurred and even less redistribution transfers
  - Except in a few cases, Government has not paid for trees on transferred land as too costly to do so. Tree crop on these properties thus remains property of ex-landowner.

3. Introductory Comments

FSA fully supports the need for land reform in as much as it can help in addressing the injustices of the past but also in promoting sustainable rural economic development and stabilising the socio-economic conditions in these areas. For these reasons FSA has, for a number of years, been proactive in developing and implementing various land reform “models” which are tailored to the conditions found in the Forestry Industry. These have been based on the need to ensure that beneficiaries run sustainable and profitable forestry enterprises. In this regard we have been extremely successful as a Sector.

On the other hand, FSA also fully supports the need for “just and equitable” compensation to be paid to those who sell their farms for land reform purposes to the State either voluntarily or involuntarily through expropriation. Conversely, we also support the need to ensure that the State does not pay inflated prices for the properties that they purchase.

Up to date the compensation paid to owners who have had their farms purchased in terms of land reform interventions by the State (restitution and redistribution) has been based on the willing-buyer, willing-seller principle. This has worked successfully and is an approach that FSA fully supports.

In terms of section 25 (3) of the Constitution:

*"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 –*
(a) the current use of the property;
(b) the history of the acquisition and use of the property;
(e) the market value of the property
(d) the extent of direct state investment and subsidy in the acquisition and beneficial capital improvement of the property; and
(e) the purpose of the expropriation."

Compensation has, in practice, thus been based on determining the market value of a property before being adjusted to take into consideration the four other factors listed above. In our view this leads to "fair and equitable" compensation being determined.

On the other hand, the Draft Regulations, given the methodology to be used to ascertain compensation payable, will result in anything but "fair and equitable" compensation being paid. Indeed, we believe that what is being proposed could very well be un-constitutional. The upshot of the Draft Regulations as they stand will be, amongst other things, to burden affected farmers with a substantial portion of the cost of land reform from their own pockets. Is this fair? In our view it is grossly unfair. If expropriation is deemed to be in *"the public interest"* then the public, through the fiscus, should foot the entire bill – not affected farmers.

We have very serious reservations about the Draft Regulations as they will, if approved, have serious direct negative impacts on our members in particular as well as indirect unintended consequences for the entire Agricultural and Forestry Sectors. In our submission we have raised some of these concerns in terms of "general comments" and then more specific concerns related to clauses contained in the Draft Regulations themselves. We trust that our comments will be viewed in a constructive manner.

4. General Comments

Listed below are a number of comments that we would like to make of a general nature relating to the Draft Regulations and which we regard as being pertinent to the debate.

4.1 Economics vs. Politics

The **"land issue"** is an extremely emotive issue and one that the Government has been battling to resolve over the past two decades. This has resulted in a plethora of initiatives and policies being developed, most of which have either been scrapped before being implemented or have proved not to be effective. The proposals currently on the table are as follows:

- Regulations in terms of Agricultural Landholdings Bill (dealing with land ceilings and foreign ownership).
- The so called 50:50 model.
- Expropriation Bill.
- Draft Regulations in terms of Property Valuations Act (PVA).

Unfortunately, more often than not, the economic issues surrounding these matters get glossed over or even ignored due to the noise generated by political rhetoric.

It is hoped that the unintended economic consequences of the Draft Regulations will not be glossed over as they will have severe ramifications for the entire Agriculture and Forestry Sectors.

4.2 Economic Impact of Willing-Buyer, Willing Seller Principle on Land Prices

As mentioned previously, the State has to date based its purchases of farms for land reform purposes on the "willing-buyer, willing-seller principle". Because the supply of land is finite, when the State gets involved in the land market in a big way, as it has, this creates increased demand and as a result thereof, the price of land tends to increase. This is simple supply and demand economics. Importantly, the price of land does not just increase in respect of those farms targeted for purchase by the State but affects the price level of all land, irrespective of whether or not the land is earmarked for redistribution or restitution. Notwithstanding this, it is debatable as to how significant the State's involvement in the land market has increased prices compared to other market forces (e.g. the deprecition of the rnd which has increased export product prices) – some arguing that these latter dynamics have had a far greater impact of land price increases.

4.3 Rationale for New Methodology for Valuing Property as Contained in Draft Regulations

The willing-buyer, willing-seller principle has come in for heavy criticism by politicians and Government officials over a number of years – their main gripe appearing to be that the State is paying "too much" for farms and hence for its entire land reform programme. These claims even go so far as suggesting that farmers are unduly benefitting from "exorbitant" land prices.

As highlighted in Paragraph 4.2 above, the State's active participation in the land market could have had an influence on the general escalation in land prices but we do not believe, however, that this has resulted in exorbitant prices being paid. The problem of exorbitant prices being paid for certain properties has nothing to do with the willing-buyer, willing-seller principle – it has everything to do with illegal corrupt Department officials.

Rather than prejudicing thousands of honest farmers through the introduction of the Draft Regulations, rather:

- check local land prices with local farmers to get an indication if the price of a subject property is in the right ball park;
- if not, get a second valuation; and
- Crack down hard on those responsible for inflating property prices through corrupt means.

There has been growing criticism of the willing-buyer, willing-seller system and this has encouraged the Department of Rural Development and Land Reform (DRDLR) to look at ways of making land reform cheaper for the Government – the 50:50 proposal and these Draft Regulations being two such examples.

It is our contention that that rationale behind the proposed methodology for the valuation of property for land reform purposes, as contained in the Draft Regulations, is purely and simply to reduce the cost of land reform for the Government.

4.4 Special Characteristics Forestry

Before considering what the possible implications of the Draft Regulations will have on the Forestry (and Agriculture) Sector, cognisance needs to be taken of its special characteristics pertinent to the proposed new valuation methodology. These are listed below:

- **Low return on investment:** Farming and forestry have very low returns on investment compared to other business activities (±5%).

- **Trees, not land, are often the greatest asset on a timber farm:** Unlike in agriculture where cash crops are invariably much lower in value than the land value, this is rarely the case in forestry. As highlighted in Paragraph 2 of this Submission, trees make up the greatest proportion of the investment in the Industry – 49.4%. This is followed by bare land at 36.9% and roads at 8.0%. The above investment in trees, however, represents a weighted average across all age classes. The value of trees as a percentage of the investment (or market value) of a timber farm can vary considerably - from a relatively low percentage if the trees are newly planted to extremely high if the trees are approaching maturity or mature. For example, forestry land on a particular timber farm could be valued at R10 000 per hectare whereas the standing value of the 25 year old pine sawlog crop growing on it could easily be R150 000 per hectare.

  Why is this a problem i.r.o. the Draft Regulations? Because, given the proposed valuation methodology whereby the value of the tree crop is added to the market value only (i.e. not to the current use value as well) before being divided by two, the loss in compensation just for the crop felt by forestry enterprises will be far greater than for agricultural enterprises. Assuming that the net use value in the above case was zero, then the owner would lose compensation of R5 000 for each hectare of land expropriated but R75 000 per hectare for the trees expropriated. Is this fair? Presumably the beneficiaries of the farm will subsequently get the full benefit of the value of the standing crop. Is this fair? In both instances, it is our view that no it is not fair.

- **Forestry is a highly risky business:** Forestry, as is the case with agriculture, is a risky business. Timber growers generally have neither control over the price they pay for their inputs nor the price they receive for their output and in addition to this, they are subject to a whole host of uncontrollable factors such as unpredictable weather conditions, pests and diseases, etc. Although the continuing drought in some timber growing areas has not yet resulted in trees dying, growth (and hence profitability) has been lost. The recent fires in the Southern Cape are another example of how vulnerable forestry is to such events –

although the final figure has not been determined, current estimates indicate that as much as 8 500 hectares of commercial timber plantations have been destroyed.

Why is this a problem i.r.o. the Draft Regulations? Because this could severely prejudice the owner of a subject property with respect to the current use value determined for the property. See comments below.

- **Net farm income is low and erratic:** As a result of the high risk associated with forestry operations, as highlighted above, net farm income is not only relatively low but highly volatile. By way of example, a summary of the results of a Case Study research project into economic returns, covering various individual agricultural and forestry enterprises and entire sectors undertaken several years by the Agricultural Economics Department of the University of KwaZulu-Natal for the KZN Agricultural Union (Kwanalu), found the following:

  - Economic profits, in those years when profits were made, were low.

  - The fact that forestry and farming was a highly risky business was demonstrated by the fact that economic profits varied dramatically from one year to the next.

  - Economic returns were often negative. Indeed, results over the entire sample of Case Studies indicated that positive economic returns were only made in 17 out of the 42 periods analysed.

  - Across all the Case Studies, the weighted average economic return made was only positive in 3 out of the 8 years covered, a mean annualised negative economic return of -2.01% being made over the 8 year period analysed.

  - Given the above, they would, on a weighted average basis, needed to have received an annual subsidy of R144 228 (equivalent to 2.84% of the weighted average value of the farms analysed) for them to have broken even over the entire period.

  Why is this a problem i.r.o. the Draft Regulations? Because, given the proposed valuation methodology based on the current use value of a farm at a specific point in time (rather than an average over a number of years), there is a reasonable chance that it could be zero – thus prejudicing the owner.

- **Forestry is a Long-Term Business:** Depending on the crop grown, the time between planting a crop and harvesting it at maturity can range from 7-8 years (gum pulpwood) to 25-30 years (pine sawlogs). The mix of age classes of trees on a particular timber estate therefore has a huge impact on cash flow and as a result, profitability in any given year.

  Why is this a problem i.r.o. the Draft Regulations? Because, as made in the point above, depending on whether a plantation was "in cycle" or not, there is a reasonable chance that its current use value could be zero – thus prejudicing the owner.

- **Farming Debt is Extremely High:** Although not broken down between forestry and agriculture, the combined Industry is highly indebted as a result of various factors such as financing input costs and more importantly, financing operational costs in those (frequent) years when operational losses are made. Between the years 2012 and 2015, farming debt increased significantly, mainly as a result of severe drought conditions being experienced during the period. In 2012 total farm debt, according to DAFF's 2016 *Abstract of Agricultural Statistics* publication, amounted to almost R88.1bn. Three years later this had exploded by R44.3bn or by 50% to a staggering R133.1bn. This has, and continues to put extreme financial strain on the Sectors as farmers battle to repay this debt. This can be highlighted by the fact that in 2015 total farm debt represented 59% of gross farm income of R225.8bn and 170% of net farm income of R78.0bn.

Why is this a problem i.r.o. the Draft Regulations? Because, given the high level of debt burden already being faced and the impact that the regulations will have on reducing land prices and thus farmers' collateral, an increase in business insolvencies could well result.

4.5 Proposed Valuation Methodology for Determining Compensation

Specific comments have been made later in this Submission regarding concerns that we have with the methodology used for determining compensation payable. In general, it is our view that the methodology is arbitrary and will not result in fair and equitable compensation being paid. The methodology will prejudice all landowners but particularly those who grow tree crops as the value of tree crops can often be a significant percentage of the total value of a timber farm – far more so than the value of cash crops as a percentage of the total value of arable farms.

The methodology used will more often than not result in the value of a farms being around 50% of their market value. However, if say, an owner had inherited rather then bought the subject property (thereby receiving *"acquisition benefits"* as defined in the Draft Regulations*)*, the application of the valuation formula could, under certain circumstances, result in a negative value for the subject property being determined. This is bizarre!

It is also concerning to note that the PVA and the Constitution refer to acquisition benefits and capital improvements by the State, whereas the Draft Regulations refer to **ANY** acquisition benefits, whether flowing from the State or not. The Draft Regulations thus need aligning with the PVA and Constitution.

Many plantations are grown on land owned by people from whom the land is rented / leased (i.e. the owner of the land does not own the trees). What would happen in the case where a subject property had a 3rd party's trees growing on the land?

4.5 Economic Impact of Proposed Valuation Methodology on Land Prices

The proposed valuation methodology will result in the value of land being eroded by a significant amount – in fact by as much as 50% for certain farms. Given the extent that the State is involved in the land market, this will distort the entire market by forcing down land prices in general across the country. The impacts of this are discussed Paragraph 4.6 below.

4.6 Economic Impact of a Reduction in General Land Prices

When looking at the implications of the proposed new valuation methodology from an economic perspective, the following well established economic principles need to be noted.

One impact leads to another and so on.

- **General land values drop:** The significant distortion of the land market which would be created by the proposed valuation methodology would result in a significant decrease in the price of land.

- **Which leads to a decrease in farmers' solvency and collateral:** As the value of land forms the basis of farmers' collateral, a reduction in land prices will result in a drop in the amount of collateral an enterprise has against which banks will be prepared to lend it money. Given the already high levels of farm debt, a reduction in an enterprise's asset base will have a profound impact on the solvency of farming enterprises. Indeed, given the quantum of the decrease in land prices envisaged, it is likely that many thousands of farmers could, virtually overnight, become insolvent.

- **Which leads to decrease in farmers' ability to finance the growth of their businesses:** The reduction in collateral available to farmers' means that their ability to raise loans is reduced. Again, given the quantum of the expected decrease in land prices, the amount that banks would be prepared to lend farmers would drop substantially.

- **Which leads to decrease in investment in fixed improvements:** This not only means that farmers will have a decreased ability to grow their businesses through investment in fixed improvements but also, in hard times such as at present, to finance working capital to keep their businesses afloat.

- **Which leads to decrease in productivity:** The reduction in investment in fixed improvements thus leads to a decrease in productivity, both in physical output and financial returns in respect of individual farming enterprises that can remain solvent. However, the decrease in productivity on those farms that will become insolvent as a result of the Draft Regulations will be 100%.

In turn, the above impacts have further unintended consequences as indicated below.

- A decrease in global competitiveness
- A decrease in food and fibre security
- An increase in bankruptcies
- An increase in job losses
- An increase in social dysfunction in rural areas including an increase in crime.

This "viscous cycle", could ultimately lead to a calamitous situation. All-in-all therefore, the implementation of the proposed valuation methodology should be halted before any damage is done and a thorough socio-economic impact assessment undertaken.

4.7 Other Economic Impacts of a Reduction in Land Prices

A reduction in land prices will also have a negative impact on the following:

- **Municipal Property Rate Income:** In terms of the Local Government: Municipal Property Rates Act (Act 6 of 2004) (MPRA), the rating of all agricultural and forestry properties was phased in and by 1 July 2008, all such properties were subject to the payment of Municipal property rates - the main determinant of rates payable being the market value of these properties. In terms of the Act, should the value of a particular property fall by 10% or more, it is beholden on the Municipality to revalue the said property at that time rather than waiting for a re-valuation when the 5 yearly general valuation roll is prepared. Should general land prices fall, as expected, this will result in decreased property rate revenue being collected by the affected Municipalities.

- **Rental Income Received by Land Reform Beneficiaries:** As mentioned previously, the Forestry Industry has developed a number of Land Reform models that have been successful in ensuring that plantations that have been transferred to claimants have remained productive assets. As a general rule, the State has only purchased the forestry land – not the trees. In these cases, the previous owner of the land invariably enters into a "lease back" agreement with beneficiaries. The rental payable to the beneficiaries is normally between 5% and 7% of the value of the land. Obviously, if land values drop, the rental income received by the beneficiaries will also drop.

- **Rental Income Received by Communities i.r.o. Leased SAFCOL Forests:** In 1992 the State's forestry assets were transferred from Government into the SA Forestry Company Limited (SAFCOL). These assets were eventually consolidated into 5 "packages" which were then put up for lease. Four of these, covering 143 000 hectares, were successfully leased out on 70 year leases. As part of the lease agreements, rental is paid by the companies owning the leases to Government who, in turn, pass this onto the communities living on these estates. Again, a drop in land values will have a negative impact on the revenue flowing from these leases back to the affected communities.

- **Capital Gains Tax / Transfer Duties:** A reduction of land prices will have a negative impact on Government's revenue receipts received from CTG and transfer duties.

4.8 Property Right Perceptions - Impact on Fixed Direct Investment in South Africa

The Draft Regulations could have impacts far beyond its original intention.

Guaranteed property rights are a fundamental tenant of any successful country – tamper with property rights and serious consequences follow – see what happened in Zimbabwe. Although the Draft Regulations deal specifically with the valuation of property that is wanted for land reform purposes rather than property rights *per se*, the fact that the proposed compensation payable for land bought for land reform purposes is a radical move away from the accepted norm, will undoubtedly create negative perceptions about the security of property rights in South Africa.

Some may see the proposals as the "thin end of the wedge" – if this valuation methodology can be used to determine compensation payable for land expropriated for land reform purposes, what could be next?

There is therefore a danger that the negative perception created could very well lead to an unwillingness by both foreign and domestic investors to invest in fixed assets locally, whether they be in agriculture or forestry or not. Given the parlous state of the local economy, Government should be doing all in its power to encourage investment to help grow the economy and create jobs, not the opposite.

4.9 Socio-Economic Impact Assessment

Given the negative impacts that the introduction of such a valuation methodology would have on the Agricultural and Forestry Sectors, as highlighted in earlier in this Submission, it is imperative that before these Draft Regulations are approved, a thorough socio-economic impact assessment be undertaken.

It is thus concerning to note that, despite these Regulations being in "Draft" form, the Valuer General (VG) published a "Manual" in August 2016 to guide valuers how to interpret the factors in the Constitution to arrive at a value defined in the PVA. However, the Manual is aligned with the Draft Regulations which introduces a new concept referred to as "current use value". The Draft Regulations propose that this should be added to the market value and divided by two. The resultant value is **NOT** considered to reflect a "just and equitable compensation" as defined in the Constitution. This needs addressing.

5. Specific Comments on Draft Regulations

5.1 Definitions: Para 1 – Current Use Value

The definition of "current use value" is stated as being:

"the net present value, as at the date of valuation, of cash inflows or other benefits that the subject property generates for the specific owner under lawful use, and without regard to its highest and best use or the monetary amount that might be realised upon its sale".

Comments:

- Sections 25(3) (a) & (b) of the Constitution both refer to the "Current Use" and "Use of the property" respectively. These clauses are repeated under the definition of value in the PVA. "Current use value" is defined in the Draft Regulations but **NOT** in either the Constitution nor the PVA. Where does the term "current use value" then come from?

  It is submitted that the definition of "use" is **NOT** the same as "current use value" and the inclusion of the definition is thus irregular. The Draft Regulations cannot include additional definitions not contained in the PVA. Again, this needs addressing.

- The determination of "current use value" is **NOT** based, as Paragraph 4. (1) of the Draft Regulations states they must, in *"accordance with generally recognised valuation practices and methods."* This is a critical flaw in the legal validity of the Draft Regulations.

- The Draft Regulations define "current use value" as the Net Present Value (NPV) of cash inflows or other benefits without regard to highest and best use or the monetary amount that might be realised upon the sale of the property. The definition does **NOT**, however, include outflows or costs despite these being included under the definition of NPV. Furthermore, the definition does not capitalise the net income. Thus, the *"current use value"* according to the definition is essentially the net profit of the property at the valuation date. Because this figure is not capitalised, the current use value is considerably lower (20 times lower at a capitalisation rate of 5%) than it actually should be. This is highly prejudicial nd needs addressing.

- It must also be noted that The Restitution of Land Rights Act deals with "rights in properties", not businesses which the Draft Regulations say should be valued.

- The Draft Regulations state that the "current use value" determination of a property must disregard *"…its highest and best use or the monetary amount that might be realised upon its sale".* Given that the market value side of the equation does take into account *"any realisable potential and assuming its highest and best use"*, is it fair to disregard these when calculating the current use value? In our view, no it is not.

5.2 Definitions: Para 1 – Net Present Value

The definition of "net present value" is stated as being:

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

Comment:

- This definition must be read in conjunction with the definition of "current use value". Please refer to the comments made under paragraph 5.5 above.

5.3 Powers of the Valuer General: Paras 2. (1) *(e) (vii) & (xiv)*

Paragraph 2. (1) *(e)* relates to what the property owner, tenant or occupier of the subject property is required to provide the authorised valuer.

Comments:

- **Paragraph 2. (1) *(e) (vii)*** specifically relates to *"financial statements".* These are confidential documents and it should not be necessary for the owner to provide such documents.

- **Paragraph 2. (1) (e) (xiv)** specifically relates to "*details of declarations of value of the subject property made to the South African Revenue Services (SARS)".* In our opinion, any documentation flowing between a taxpayer and SARS is confidential and that as such, there should not be a requirement to supply the authorised valuer with such declarations.

5.4 Valuation Practices, Methods, Standards and Procedures: Para 4. (1)

This paragraph states that:

"All valuations in terms of the Act and these regulations must be conducted in accordance with generally recognised valuation practices and methods."

Comments:

- This is ironic to say the least as the proposed methodology used to determine the *"current use value"* of a property is most certainly not in accordance with generally recognised local or international valuation practices and methods!

- It should be noted that the International Valuations Standards Council lists six methods that can be used to determine value - “current use value” is not one of them.

- Of concern is that it appears that Paragraph 7. of the Draft Regulations, giving the VG the power to issue directives i.r.o. valuations, can override Paragraph 4. (1) – see comment under paragraph 5.13 below. This conflict needs addressing.

5.5 Procedures for Valuations of Property Identified for Purposes of Land Reform: Para 5. (1) (a)

This paragraph states that:

“the authorised valuer shall determine the ***current use value*** *of the subject property as at the valuation date”.*

Comment:

- As a valuation would be done on a specific date and given the circumstances pertaining to the Sector *vis à vis* lumpy cash flows, there is a reasonable chance that the “current use value” would be zero, but almost certainly less than market value, which would thus greatly prejudice the owner.

5.6 Determination of the Value of the Subject Property: Para 6. ***(a)***

This paragraph states that the valuer shall determine the value of the subject property for the purposes of section 12(1)(a) of the Act by:

“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”.

Comments:

- It would appear that the equation is completely arbitrary. How was it arrived at?

- The net result will be that compensation payable will be between 50% and 100% of market value but in all likelihood and in most cases, closer to 50% of the market value.

- In essence, a substantial portion of the cost of land reform will be transferred from the State to those individuals whose properties are bought by the State for land reform purposes. This is neither fair nor equitable. Our view is that if “land reform” is deemed to be in the “public interest”, then the public should fund it – this being done through the fiscus.

5.7 Determination of the Value of the Subject Property: Para 6. ***(b)***

This paragraph states that the valuer shall determine the value of the subject property for the purposes of Section 12(1)(a) of the Act by adding the current use value of the property and market value of the property and then dividing by two……

*"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 must be added to market value before the division referred to in paragraph (a) is performed……".*

Comments:

- Given the formula for determining the value of a property, adding the value of moveable property, annual crops and timber **ONLY** to the market value side of the equation would, in effect mean that the State would only pay compensation in respect of tree crops amounting to 50% of the market value of these biological assets. Given the high value of trees as a percentage of the market value of forestry estates, as much as 25% of the market value of a forestry property could be wiped out. This is unacceptable.

- Regarding growing timber, as mentioned previously, this 50% loss in value would invariably cost the timber grower significantly more in lost compensation than that lost on the value of the land upon which the trees were grown. Given the significant potential value of the timber crop, timber growers would be prejudiced far more than those growing annual crops due to the differential in the value of the respective crops in relation to land values.

- No mention is made in the Draft Regulations as to how growing timber and annual crops should be valued. We recommend that this be included (e.g. for growing timber, the Faustmann method should be used).

5.8 Directives for the Valuation of Subject Property: Para 7.

This Paragraph states that:

"All valuations in terms of the Act, shall be conducted subject to such directives as may be issued by the Valuer-General generally or in respect of a particular valuation."

Comment:

- Foresty South Africa's members have informed the Association that they have been requested to provide copies of their financial statements to valuers for the purposes of valuing their properties for land restitution purposes. It appears that these have been requested for the purposes of determining the "current use value" of their properties as defined in the Draft Regulations. It is apparent that the VG has already issued directives to valuers on how to determine the "current use value" as contained in the Draft Regulations and "Technical Manual" produced by the Office of the VG (OVG), which are essentially based on an unconventional "income" approach to value.

- Furthermore, unlike the standard EBITDA method of valuing properties, interest, taxes, depreciation and amortisation are apparently **NOT** to be deducted from gross income. This, in effect, reduces the net income of a property upon which a capitalisation rate is applied, thereby prejudicing the owner. This is in conflict with Paragraph 4. (1) which stipulates that all valuations **MUST** be conducted in accordance *with "generally recognised valuation practices and methods."* It would thus appear that directives issued by the VG are in conflict with *"generally recognised valuation practices and methods."* This is unacceptable and needs addressing.

5.9 Representation by Owner or Person in Charge of Property: Para 9. (5)

Paragraph 9. deals with cases where the owner of the property disputes the valuation of his or her property. Paragraph 9. (4) states that following representations from the owner and valuer, the VG may "adjust the valuation and certify the valuation certificate as final".

Paragraph 9. (5) then goes on to state that:

"The Valuer-General shall deliver the final valuation report and valuation certificate to the instructing authority."

Comment:

- In Paragraph 5. (b) of the PVA, the Valuer General **MUST** be impartial and **MUST** exercise the powers and perform the duties of the Office without fear, favour or prejudice. Thus, the VG should not make any adjustments to any valuations or valuation certificate certified by the valuer who undertook the instruction. The Valuation Report, produced by the valuer, after inspection by the valuer and the OVG, should be the final Valuation Report and Certificate which should be delivered to the instructing party. In the event of litigation, it is this Valuation Report which will be relied upon and the VG cannot produce his own Report or Certificate unless he conducts the valuation himself.

7. Concluding Comments

7.1 Summary of our Views

Although it is stated in Paragraph 4. (1) *that "All valuations in terms of the Act and these regulations must be conducted in accordance with generally recognised valuation practices and methods.",* the Draft Regulations then go on to make provision for the valuation of properties on the basis of a methodology which is most certainly **not** a generally recognised valuation practice or method.

Furthermore, not only do the Draft Regulations provide for a valuation methodology which is not a *"recognised valuation practice or method"*, in our view:

- the methodology is based on a flawed "current use value" basis;
- the determination of value by adding the current use value and market value together and then dividing by two is totally arbitrary;
- will result in compensation payable being far from *"fair and equitable";* and
- are not consistent with the provisions of Section 25 of the Constitution or those of the PVA.

The bottom line is that we believe that the Regulations are purely an attempt by Government to reduce its land reform costs and if implemented, will, quite frankly, equate to nothing more than legalised theft.

7.2 Summary of our Recommendations

- First and foremost, the Draft Regulations, as they stand at present, should be scrapped in their entirety and re-drafted from scratch.

- When re-drafting the regulations, cognisance of international best valuation practice, as promoted by the International Valuations Standards Council, should be taken as well as the contents of the FAO's report on "Compulsory Acquisition of Land and Compensation" which promotes the principle of "equivalence" when determining compensable payable. This states that those impacted by expropriation should be neither better nor worse off afterwards with compensation being based on the fair value of land and improvements as well as compensation for any negative livelihood impacts.

- The re-drafted Regulations must:

  (a): result in affected owners being paid "fair and equitable" compensation;
  (b): adhere to international best practice;
  (c): result in valuations being conducted in accordance with "generally recognised valuation practices and methods"; and
  (d): be aligned with Section 25 of the Constitution and the provisions of the PVA.

- For the purposes of calculating compensation payable, the value of tree crops should be treated separately and compensated for in full.

- Valuing forestry and agricultural properties is a highly technical and skilled undertaking. Currently, there are relatively few valuers in the country who specialise in this field and are thus competent to value forestry and agricultural properties properly. It is thus recommended that the VG only use these valuers to conduct the valuation of these properties until such time as other valuers are trained up to undertake these specialised valuations.

- Before any regulations dealing with the valuation of subject properties for the purpose of land reform are adopted, a full Socio-Economic Impact Assessment needs to be undertaken.

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14th June 2017