The International Valuation Standards Council's Exposure Draft on the Valuation of Forests

INTRODUCTION

1. The Institute of Chartered Foresters (ICF) is the Royal Chartered body for forestry and arboricultural professionals in the UK. Our members practice in every branch of forestry and arboriculture relating to forests, woodlands and trees. We provide services to members including support and promotion of the work of foresters and arboriculturists; information and guidance to the public and industry; and training and educational advice to students and professionals looking to build upon their experience. We also regulate the standards of entry to the profession and offer examinations for professional qualifications. We are regulated by our Royal Charter and maintain a Code of Ethics and Rules of Professional Conduct for all members.

2. The vast majority of professionals involved in valuing woodlands in the UK will be members of the ICF and their views are represented here.

3. We support the development of an international standard for the valuation of forests and we are pleased to have the opportunity of commenting on the draft. We welcome the opportunity to comment on the exposure draft, but we have only recently been aware of its existence and therefore our comments are of necessity fairly brief and focus on valuation principles rather than on some of the detailed technical issues connected with valuations based on applying compounding or discounting techniques.

4. Our comments are based on valuing woods in the UK, but we are aware that one of the challenges of developing an international standard is the very wide variation in practices in different countries and in the development and sizes of national markets for woodlands and forests. Further difference in values may occur because of differences in the fiscal and financial frameworks that forestry and other land users operate in different countries. In the UK the woodland market is relatively small, but is well established.

5. Forestry valuation is a specialist area that requires experience in the sector. The variables are complex with comparable valuation methods constrained by the low number of transactions of similar properties. Whilst on a global basis there may be merit in a standard format for valuing large tracts of productive forest, in a UK context there are layers of influence from amenity, sporting, tax etc that confuse the simplicity of a discounted cash flow. It is not clear how an international standard will be interpreted in different countries considering that the definition of Market Value is the price between a willing buyer and a willing seller.

6. Obtaining information on the prices for which woodlands sell for can be difficult and this is often given as a reason for not valuing woods on a comparative market value basis as is used in agriculture, domestic houses or commercial property. Valuing woodlands is therefore a specialist activity. In contrast compounding and discounting techniques are much more widely known to foresters and those in the finance industry which tends to result in them being much more widely applied without the necessary expertise. Training and experience are therefore essential.
ANSWERS TO QUESTIONS

7. **Q1.** Valuations based on comparative market values can be applied to a wide range of different types of woods, both commercial and non-commercial, and to both large and small woods if there is a reasonably active woodland market as there is in the UK.

8. **Q2i.** The TIP is narrowly focused on describing the different methods of valuing forests and some of the issues and assumptions that arise from applying different mathematical methods of calculating values. What is required is guidance on when it might be appropriate to apply the different methods. In some countries where there is no active woodland market there is no alternative to valuing woods other than by calculating values by compounding or discounting certain values at a particular discount rate. In other countries where there are sales and purchases of woods there are market values and so these should be used as compounding or discounting values can give incorrect, anomalous and in some cases misleading values. **The Standard should emphasise the importance of using market values as the main basis of valuation and only departing from this when a market does not exist or there is evidence that it is so imperfect that it is unreliable.** Unless no woodland market exists any market values should be shown along with any calculated forest or woodland values. The crisis in the banking sector has been partly caused by valuing assets using mathematical techniques rather than market values, for example.

9. **Q2ii.** We think it is not necessary for the TIP to detail the sampling and measurement techniques that must be used, but it should be mandatory for valuers to clearly specify what sampling and measurement methods they have used and to explain why they have used them. Where possible sampling errors should be calculated and shown if trees volumes are to be measured as part of the valuation process.

10. **Q3.** In the UK comparative market valuations are used to value woods and forests because there is a small but active woodland market i.e. values are deduced from what similar forests or woods have sold for. A DCF is frequently used to provide the valuer and purchased with some additional supporting information. Comparative market valuation principles are applied when valuing trees of all ages, although close to maturity or likely time of felling, the value of a wood is heavily influenced by the timber content of the stand or forest. It is wrong to suggest that we would compare bare land with a restocking liability with agricultural land, probably better to remove the highlighted sentence completely.

11. **Q4.** No.

12. **Q5.** There is no necessity to require the use of a specific length of time for a forecast as the most appropriate one will vary according to circumstances. However we think it is most important that the period that has been adopted is clearly specified and the reason for its adoption explained.

13. **Q6.** We agree that greatest weight should be given to market based inputs. In the case of interest rates we would suggest that ‘bank rate’ might be an appropriate starting point for deciding on what interest rate to use when calculating values mathematically. We would suggest that a valuer departing from that rate should explain why a different rate is being used e.g. additional risk premium etc.

14. **Q7.** Compounding establishment costs can be used in the absence of market values, but it can result in very misleading values. Where there is an established woodland market there can be quite significant divergence in values for young woods and the differences
can increase over time. For example, land values can fall be up to one third after trees are planted on land previously in agricultural use.

15. **Q8.** If values are changed from time to time simply by using a different basis of valuation there must be a clear rationale for doing so. Transparency is vital so that the owner / companies / investors can come to their own views as to the appropriateness of the change in valuation method. We consider that the Standard should specify that the best case valuation method to adopt is one based on comparative market values and if there is to be a departure from this it should be fully explained and justified.

16. **Q9.** If the ownership of a tree crop is separate from the land, and the land is leased, then it would be appropriate to value the trees independently from the land. If the valuation is being undertaken for an owner or company that owns both the trees and the land then there is little justification in valuing the two separately. Capital is invested in both and the trees cannot exist without the land (as Q3) The difference between the market value of a forest or wood and the comparative market value of the land is the value that can be attributed to the trees. This cannot be a precise calculation because there are very few comparables (possibly none) of bare land being sold with a forestry restocking commitment.

17. **Q10.** This apparent anomaly only occurs when using values calculated using compounded costs or DCF techniques and it indicates the limitations / pitfalls when relying on them rather than market values.

18. **Q11.** We think the TIP might benefit from providing guidance as to when the different valuation methods might be used and to emphasise in undertaking valuations that the valuer:
   - Requires clear instructions which specify what the purpose of the valuation is.
   - Should adopt a comparative market value approach when valuing woods and forests.
   - Clearly explain the reason for adopting values calculated by compounding costs or DCF analysis. In doing so the available market values should be specified as well in any report however limited they may be.
   - Fully explain the sampling and measurement techniques that have been used and why along with estimates of any sampling errors.

19. Given the limited time we have had to comment on the draft, we are aware that there are limitations in our response. We would be pleased to provide further information or a more detailed explanation if required.