

## International Valuation Guidance Note No. 10

### Valuation of Agricultural Properties

#### 1.0 Introduction

- 1.1 In many regions of the world, lands devoted to the production of agricultural commodities are the major economic asset and, frequently, the sole economic base of a region.
- 1.2 Lands devoted to agricultural use are thus a principal subject of valuation services for a multitude of reasons including private and public transfer of ownership, taxation, determination of collateral for financing, and economic, land-use, and investment studies. Reliable valuations of agricultural lands are essential to ensure the availability of capital necessary to support the continuity of the economic base, to promote the productive use of the land, to maintain the confidence of capital markets, and to meet the needs for general financial reporting.
- 1.3 Providing reliable and accurate valuation service for agricultural properties requires that the Valuer have a sound knowledge and understanding of the physical and economic elements that affect the productive capacity of agricultural lands and the value of the commodities produced thereon.
- 1.4 The physical and economic characteristics of agricultural lands differ from those of non-agricultural or urban environments in degree of importance.
  - 1.4.1 Soils in an urban environment must be suitable for bearing the improvements that stand upon them. In agricultural properties, the soil is the principal agent in production, varying in its capacity to support a given amount of a particular commodity or class of commodities.
  - 1.4.2 In urban environments, the economic use of a property and/or the amenities it provides may remain unchanged over a period of years and may even be guaranteed by contractual arrangements. While for some agricultural properties, the

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same use may extend over a long duration (e.g., forests harvested after 25 years), for others, the economic benefits can vary from year to year, depending on the commodities the property is capable of producing.

- 1.4.3 The income stream associated with agricultural property will vary from year to year, depending on the type of agriculture for which it is used, the commodities produced, and the cyclical nature of the commodity markets.

## 2.0 Scope

- 2.1 This GN encompasses

- 2.1.1 Those characteristics of value associated with agricultural properties, and

- 2.1.2 The basic requirements of the Valuation Standards and Applications as they apply to the valuation of agricultural properties.

## 3.0 Definitions

The agricultural uses of properties may be classified in several broad groups, definitions of which follow.

- 3.1 *Crop(ping) Farms.* Agricultural properties used for growing commodities that are typically planted and harvested within a twelve-month cycle. Properties used for annual crop production may grow more than one type of annual crop over the same period and may or may not make use of irrigation to produce the crops. Some commodities are *annual crops* that may be left in the ground beyond a twelve-month cycle, per contract provisions or in circumstances where market conditions are unfavorable. These crops will last for more than one year after harvest but are considered less than permanent. Also see *irrigated land, perennial plantings*.
- 3.2 *Irrigated Land.* Lands used to produce crops or forage for livestock and which require the application of water other than that from natural rainfall are called *irrigated crop(ping) farms* or *irrigated graz-*

*ing land.* Properties that lack a water source other than natural rainfall are referred to as *dry land agricultural properties*.

- 3.3 *Perennial Plantings.* Crops grown from plantings that have a life extending beyond one year or one crop cycle. Examples are vineyards and orchards. These types of properties can have significant capital investment in the plantings, which represent a depreciable asset. Also see *forestry/timberland*.
- 3.4 *Specialised Livestock Facilities.* See *dairy farms, livestock ranches/stations*
- 3.5 *Livestock Ranches/Stations.* Agricultural properties used to raise and feed animals such as cattle, sheep, pigs, goats, horses, or combinations thereof. The actual use of these properties can take many forms. The animals may be bred, raised, and sold within the operation of the property. Young animals may be acquired from outside the property and then raised within the property. The animals may be raised for consumptive use or for breeding stock. Feed for the animals may be produced on the property, imported, or supplied by both sources. Properties used for the production and feeding of livestock have significant capital investment in the structural improvements (pens, livestock shelters, sheds, division fencing) and the livestock, which may or may not be depreciable depending on the laws and regulations of the local jurisdiction.
- 3.6 *Dairy Farms.* Agricultural properties used for the production of milk from cows or for other dairy products. These properties usually have extensive structural improvements (barns, milking parlours, silos) and equipment (feed bins, milking machines). Feed may be produced on the property, imported, or supplied by both sources.
- 3.7 *Forestry/Timberland.* Agricultural property used for the growing of non-orchard trees that are periodically harvested over extended growing periods (10 to 20 or more years). Considered to be agricultural properties because they produce a *crop*, i.e., wood, even though that crop requires a long-term growing period. Also see *perennial plantings*.
- 3.8 *Specialised, or Special Purpose, Properties.* Agricultural properties that do not typically produce a crop but are used for the handling,

processing, or storage of crops following harvest. These properties frequently have a small land base that is extensively developed with structural improvements (grain elevators) and equipment (lifting machinery). Properties may also be classified as *special purpose* by the nature of the commodity produced. Examples are truck farms, poultry farms, farms that produce certified crop seeds or fresh cut flowers, and racehorse breeding or training stables.

- 3.9 *Integrated Unit.* An agricultural entity that has common ownership of all or part of the processes involving the production and marketing of its products and/or commodities.

#### International Accounting Standards Definitions

- 3.10 *Agricultural Activity.* Management of an enterprise for the biological transformation of living animals or plants (biological assets) for sale, into agricultural produce, or into additional biological assets. (See International Accounting Standard 41 [IAS 41], Agriculture.)
- 3.11 *Biological Assets.* Living animals or plants raised for sale, to be transformed into agricultural produce or into additional biological assets (IAS 41).

### **4.0 Relationship to Accounting Standards**

- 4.1 International Accounting Standards 16 (Property, Plant and Equipment), 40 (Investment Property), and 41 (Agriculture) apply to the valuation of agricultural property. An entity follows IAS 16 or IAS 40, depending on which standard is appropriate in the circumstances. IAS 16 requires that land be measured either at its cost less any accumulated depreciation and accumulated impairment losses or at a revalued amount. IAS 40 requires land that is investment property to be measured at its fair value, or cost less any accumulated depreciation and accumulated impairment losses. IAS 41, which establishes no new principles for land related to agricultural activity, requires that biological assets physically attached to land (e.g., trees in a plantation forest) be measured at their fair value less estimated point-of-sale costs, separately from the land.
- 4.2 IAS 41 acknowledges that there may be no separate market for biological assets attached to the land but that an active market may exist

for the combined assets, i.e., the biological assets, raw land, and land improvements, as a package. An entity may, therefore, use information regarding the combined assets to determine fair value for the biological assets. The fair value of raw land and land improvements may be deducted from the fair value of the combined assets to arrive at the fair value of the biological assets. (See IAS 41, para. 25.) IAS 41 also gives guidance on how to determine fair value for a biological asset or agricultural produce where an active market exists as well as in the absence of an active market.

4.3 Agricultural property assets can be classified as:

- Land
- Structural improvements
- Plant and machinery (attached to the land)
- Plant and machinery (not attached to the land)
- Biological assets (attached to the land)
- Biological assets (not attached to the land)

The *Fair Value/Market Value* of biological assets is the contributory, or added, value they give to the land. IAS 41 requires that biological assets be measured upon initial recognition and at each balance sheet date.

4.4 IAS 16 recommends frequent revaluations, stating that every three to five years may be sufficient. IAS 40 requires revaluation on an annual basis.

## 5.0 Guidance

5.1 **Diverse forms of commodity production and methods of operation are characteristic of agricultural properties. These properties may also represent various combinations of land, buildings, equipment, and crop plantings. Generally accepted valuation principles (GAVP) are as applicable to agricultural properties as they are to the valuation of other forms of real property.**

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- 5.1.1 The Valuer must have competence in valuing the various assets that comprise the property. (See IVS Code of Conduct, section 5.0, Competence.)
- 5.2 **Market Value must be recognised as the fundamental basis of valuation (IVS 1).**
  - 5.2.1 The Valuer shall arrive at the *Market Value* for the agricultural property, ensuring that the valuation is market-derived.
  - 5.2.2 For financial reporting, the Valuer shall apportion the *Market Value* in accordance with the requirements of the IAS. For guidance, the reader is referred to IVA 1.
- 5.3 **Where other bases of valuation are used, they must be distinguished from the *Market Value* basis.**
  - 5.3.1 When estimating values other than *Market Value* as required for financial reporting, depreciation schedules, or tax purposes, the Valuer must ensure that the distinction is clearly defined and noted.
- 5.4 **Non-Realty Elements**
  - 5.4.1 When the valuation is made of an agricultural property that may include *non-realty elements* such as livestock, stored crops, and equipment, the Valuer needs to understand when a crop or other commodity is real property and when it may become personal property. Timber for example, is part of the real property while growing but becomes personal property when it is removed from the land.
- 5.5 **The Valuer must understand the unique nature of agricultural productive factors, commodity markets, production practices, and cycles in the market region.**
  - 5.5.1 In the valuation of agricultural properties, the physical and environmental aspects of the property assume special importance. These include features such as climate, soil types and their productive capability, the availability or absence of water for irrigation, and the feeding/carrying capacity for

livestock. External factors to be considered include the availability and adequacy of support facilities required for storage, processing, and transportation. The relative importance of these factors will vary depending upon the type of agriculture for which the property is suited or used. The Valuer needs to consider both internal and external factors in making a determination of which class of agriculture use the property is best suited for.

5.5.2 In keeping with the definition of *Market Value*, a *highest and best use* analysis of the property should always be conducted in order 1) to warrant that an agricultural use is to be continued, especially when it appears that another land use, e.g., subdivision development occasioned by encroaching urban/suburban expansion, might be more appropriate, and 2) to determine whether the specific agricultural use is to be continued.

5.5.3 Where the Valuer is specifically instructed to ignore uses other than the current agricultural use, the resulting valuation will not necessarily indicate the *Market Value* of the property, and this should be fully disclosed.

**5.6 The estimate of stabilised income to the agricultural property must be based on the crop patterns and cycles in the market area.**

5.6.1 The cash flow to agricultural properties is a function of both the production cycle followed on the property and cyclical forces such as commodity markets. The Valuer should understand the impact of these cycles on cash flows. The valuation of the property must be based on the stabilised pattern of income that is consistent with the production cycles commonly practiced in the region in which the property is located.

**5.7 The Valuer of agricultural property that has more than one physical component or class of agricultural use must clearly state whether the value of each component or use is its value contribution as part of the whole property or its value as a separate, free-standing component.**

- 5.7.1 The various components of a whole property may have value as separate parts which is greater or lesser than their value as part of the whole. The Valuer must determine whether each component is to be valued individually or as part of the whole property.
- 5.7.2 Agricultural properties may be managed to simultaneously produce more than one class of commodity based on different physical conditions within the property or on management decisions. In the valuation of agricultural properties on which crops of more than one agricultural classification are cultivated and harvested at different times, the value of each agricultural classification must be based on its contribution to total property value and not its stand-alone value.
- 5.7.3 The agricultural use of the property may require extensive building improvements, e.g., barns, silos, dairy machinery. Such improvements, while requisite to the proper operation of the property, are frequently secondary to the principal land asset. Their value must be based on their contribution to the total value of the property regardless of their cost or other measure.

Typically, such improvements have a value in use, i.e., their contributory value to the enterprise/entity. On those occasions where an allocation of value between the assets may be required, such an allocation is not to be taken as an indication of the individual value of the improvements as separate assets.

**5.8 The requirements for valuation reports are addressed in the IVS Code of Conduct and IVS 3, Valuation Reporting.**

**6.0 Effective Date**

- 6.1 This International Valuation Guidance Note became effective 30 April 2003.