A REVIEW OF UNIFORMITY IN PROPERTY RATING VALUATION IN NIGERIA

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Abstract

Property rating valuation is a statutory practice backed up by law. In Nigeria and many other countries that adhere to the UK property rating practice, the standard methods of valuation adopted are the comparison, the depreciated replacement cost and the profit methods. These methods however, have some inherent challenges which often lead to variation in valuation. Variation in valuation has been identified as one of the major problems hindering the optimal benefits derivable from property tax. Using an in-depth literature review, this paper identifies the potential input variables in the three methods of valuation that may cause variation in rating valuation. It also examines the causes of disparity among valuers in Nigeria from the comparison of the provisions of Kwara State and Oyo State tenement rating laws on these input variables. The study identifies between two and five input variables in the comparison, profit and contractor’s methods that may produce the observed variation in rating valuation in those methods. The study also reveals that Kwara State may be more prone to non-uniformity of valuation than Oyo State due to the subjective nature of the input variables. The study advances that this form of non-uniformity if uncorrected, may lead to low revenue yield, litigation and protests in practice. The study recommends that the two States concerned and their local authorities should seek amendments to the existing rating laws through the various Houses of Assembly, and that the States should adopt other best practices of other counties on uniformity of valuation in order to improve rating valuation practice in their respective domains.

Keywords: Rateable value, statutory valuation, Tone of the list, Valuation variation

1.0 INTRODUCTION

One of the reasons for carrying out valuation is taxation. The standard practice for property rating valuation, which is recognised by the valuation standards of some other countries, is the rating law (The Australian Property Institute and Property Institute of New Zealand, 2012; BOVEA, 2015). Consequently, a tax law must be explicit in guiding the policy and administration of property rating within a rating area, to ensure a uniformity of valuation (Babawale and Nubi, 2011; Oni and Ajayi, 2011; Atilola, 2013). This practice in Taiwan shows that the tax law is not explicit to ensure uniformity of valuation among valuers (Lin, 2010). This shows that what was experienced in Taiwan is also prominent in some of the property tax laws in States like Lagos, Oyo and Kwara, among others in Nigeria (Tomori, n.d; Babawale, 2013; Atilola, 2015).

Although there are various methods of valuation, it appears there are only three methods that usually appear to be generally adopted in many States’ rating laws in Nigeria (Atilola, 2015). These three methods of rating valuation are; the depreciated replacement cost described by Bond and Brown (2011), as the
method of last resort, used to value all property types the comparison and profit methods (Rayner, 1985; McCluskey and Franzsen, 2005; Shapiro et al., 2009; Bond et al., 2011). Since rating valuation is a statutory valuation, it is expected that the statute to be applied on the procedures and principles that will be adopted for the valuation. Not only this, it is expected that the law will specify the data to be used or, alternatively, the development of the ‘Tone of the List’ as the practice in Tanzania and Botswana where the cost of construction, depreciation and land value among other are given (Kayuza, 2006; Leima and Svensson, 2014). The need for appropriate data specification in property rating law for the purpose of assessment of a hereditament becomes therefore, very important, since it provides the basis for uniformity of valuation (Bond, 2012). The implication of the above assertion is that the content of the tax law helps to improve on the level of variation in valuation among valuers.

One of the reasons that are often advanced for variation in valuation is the choice of methods adopted by valuers, and the peculiarity of the data that are applied to each method (Kuye, 2003; Ogunba and Ojo, 2007; Ayedun, 2009; Lin, 2010; Babawale and Omrin, 2012). Bond et al. (2011) posit that a 1% difference in the decapitalisation rate that is one of the input variables among valuers could resulted to 20% variation in the final value. In property taxation, these issues manifest mostly when the law has no specification for the valuation methods, and the input variables for each method. In a bid to achieve high level of uniformity of valuation and less variation in valuation in Tanzania, for example, the rate of depreciation is graduated for all property types (Kayuza, 2006). The adoption of this kind of statutory depreciation rate will, no doubt, reduce the incidence of variation in valuation, which could have occurred in the case of depreciated replacement cost method. Whereas on the contrary, in rating law that the variables were not standardized might witness very high level of non-uniformity of valuation and variation in valuation among valuers.

The study examines the three methods of valuation used for property rating in Nigeria with a view of identifying the ‘input variables’ in each method, which cause variations in rating. Also, this study attempted to investigate whether the provision or mechanism exist in the laws to ensure a uniformity of valuation outcomes among the practitioners. In doing this, the study compares the Local Government Tenement Rates Law 2006 of Kwara State and the Oyo State Tenement Rates Cap. 160 of 1995. The reason for adopting the two States is based on the replication of the laws after the Nigerian Legal System from the Colony of Lagos, the laws of the Southern and Northern Protectorate of Nigeria, the Regional Government, and up to the state creation exercise of 1967 (Obilade, 1979). Kwara State, being part of the Northern Protectorate, represents the North, while Oyo State being part of the Southern Protectorate, and represents the South for this study. These two States were created in 1967. Uniformity of valuation in this study is seen from the perspective of where two independent valuers use or adopt the similar value input variables and secondly, whether they arrive at the same or similar rateable value on a hereditament.

2.0 REVIEW OF LITERATURE ON INPUT VARIABLES IN VALUATION METHOD

The three methods of rating valuation recognised by most Nigerian valuation rating statute books are the comparison, the depreciated replacement cost, and the profit methods (Section 16, 19 & 21 of the Local Government Tenement Rates Law (LGTRL), 2006 of Kwara State; Section 24, 25 and 27 of Oyo State Tenement Rates Cap. 160 of 1995). There are eight input variables that are needed for the valuation from these three methods of valuation. Since rating valuation is a statutory practice, the input variables need to be specified either by the rating law expressly, or given the responsibility to a Statutory Officer to prescribe, as and when due, as is the practice in the UK, Australia and Tanzania (Rayner, 1978; Butler and Richmond, 1990; Kayazu, 2006; State of Queensland, 2010; Bond et al., 2011).

According to Lin (2010) the input variables needed in statutory valuation can be grouped
into two. These are market input variables and institutional input variables, the first category being determined by the forces of demand and supply, while the second is stated in the law as guidelines or regulations for the assessment (Kayuza, 2006; Bond et al., 2011). In property rating, these variables are expected to be documented in what is called the ‘Tone of the List’, which forms the basis for the Valuation List (State of Queensland, 2010; Bond, 2012; Leima et al., 2014). The market input variables consist of the gross rent, cost of construction, land value, and divisible balance. The institutional variables are depreciation rate, decapitalisation rate, tenant share, and outgoings.

In the three methods of valuation, outgoings appear to be a common variable, and it represents a variable in valuation for annual value. The outgoing is deducted from the gross rental value to get the rateable value. In the UK, under the General Rate Act of 1967, Section 19(2), and the Valuation (Statutory Deductions) Order 1973, the outgoing rate is graduated in table called ‘statutory deductions to convert gross value to rateable value’ (Rayner, 1978). Bond et al. (2011) posit that the outgoing comprises of the external repair and insurance, when the hereditament is let on internal repairing lease term. However, the use of this table has come to extinction in the UK from the time the basis of valuation has changed to net annual value from the gross annual value. There is therefore no more provision for outgoings in the UK practice; rather, the gross annual value is determined by market forces. For there to be uniformity, some local authority value band on various types of hereditaments in the rating area (Muhammad et al., 2012; Babawale, 2013; Leima et al., 2014). However, the use of value band has been questioned by some experts on the basis of possible errors, particularly in countries where this is applied to non-prototype hereditaments (Babawale, 2013).

In his contribution, Kayuza (2006) posits that the observed uniformity of rating valuation, which characterises Tanzania, is due to the fact that the rating valuation assessment guidelines have been standardized by providing the ‘cost per square meter’ for all types of property to be assessed. Also, the Tanzania rating law specifies the range of value for the depreciation rate. Depreciation, as a factor affecting the depreciated replacement cost method of valuation uniformity, has been criticized on two grounds. The first criticism centres on the method of depreciation adopted, as there are about five basic conventional methods of depreciation that valuers may choose form (Ifediara, 2000; Andrew and Pitt, 2006; Ogunba, 2011; Bello, 2014), while the second is the appropriateness of determining the rate of depreciation. Ogunba and Ojo (2007) have argued that valuers often use different depreciation rates for the same property. But these two criticisms can be merged into one, once the depreciation rate is given. Apart from the above, the sources for the cost of construction adopted by valuers are also a matter of concern (Ojo, 2004; Ogunba et al., 2007). The land value to be used in the DRC method is determined by the forces of demand and supply. However, in countries where there is no property data bank and the land value is not given in the tone of the list, its determination is as at the judgment of individual valuers (Kayuza 2006; Lin, 2010).

This practice in Tanzania is similar to what obtains in Botswana, where there are benchmarks for price per square meter for land and improvements (Leima et al., 2014). However, land value in England is determined on the principle of ‘rebus sic stantibus’ at the market value, not on highest and best use. Also in England, statutory decapitalisation rate of 5% to 3.3% is used to derive at the gross rental value for non-domestic hereditament, as this is contained in the 2004 Regulation (Bond et al., 2011). However in Hong Kong the decapitalisation rate is determined by the property market yield as contained in Section 7(2) of the Rating Ordinance (Brown, 2013).

On the issue of divisible balance in profit method, Kuye (2003) argues that, the book from where it is determined is not available in many instances, and when they are, the information may not be sufficient for the exercise. The difficulty in ascertaining the books of account of business operators has resulted to the use of value banding of 1star to 5 stars for the hotels in Ipoh as a means of determining the divisible balance (Muhammad et al., 2012). This
approach was introduced to the rating administration in Ipoh (Perak State) to ensure uniformity of valuation among various hotel categories.

The other issue that is of concern in profit method is the determination of the tenant share from the divisible balance. However, Brown (2013), has identified four ways of determining the tenant’s share, whereas, Bond et al. (2011) suggests five ways. The four that is common to both authors are: a percentage return on tenant’s capital; a percentage of gross receipts; a proportion of the divisible balance and a spot figure. The fifth is the use of individual figures for remuneration, risk and interest on capital. It seems there is no consensus on the appropriate tenant share method, as Courts’ discussions on this matter have favoured virtually all the methods (Bond et al., 2011; Brown, 2013).

3.0 METHODOLOGY

The main objective of this paper is to examine the similarities and differences between provisions of Kwara State and Oyo State tenement rating laws on the valuation input variables. These input variables were identified from the literature as some of the potential factors which are causing disparity among valuers. Hence, the focus is on uniformity of valuation that is achievable in the input variables, which ought to have been either expressly prescribed or having the responsibility or imposing on a Statutory Officer in Nigeria. The content of the Kwara State and the Oyo State Rating Laws were explored and compared for their similarities and differences with reference to the input variables. That data are presented in tables and figures, conveying the descriptive nature of the analysis.

4.0 RESULT

The intention of the two States is to ensure uniformity of valuation. Section 22 of the Local Government Tenement Rates Law stated that:

*For the purpose of ensuring uniformity of assessment the appraiser shall, in determining the rateable value of a tenement, either by reference to annual rent or current replacement cost, have regarded to the level of the rent prevailing in the locality for the particular type of tenement or of the building/structure costs in the locality for that particular class of tenement or a fair charge for the particular type of occupied quarry mineral sites reflecting comparative market value of such mineral.*

More so, section 28 subsection 1 and subsection 2 states that:

*An appraiser shall ensure uniformity of assessment in determining the rateable value of tenement, either by reference to annual rent or current replacement coast.*

*He shall take into consideration the particular type of tenement or of the building costs in the locality in which what particular class of tenement is situated.*

The provisions of the two states’ statutes are similar in the aspect of guaranteeing uniformity of valuation. Also in its principles and procedures of the methods the two statutes are similar. In Table 1 (Appendix 1), the details of the statutes for the input variable are presented. The input variables are discussed in detail in subsequent section of this paper as to ascertain uniformity of valuation is achievable with the content of the rating laws in the two states.

5.0 DISCUSSION

In sections three and four, the 8 input variables in the 3 methods of property rating valuation has been discussed. In this section, a critical view of the variables in each method of valuation with a view of exploring the provision of the law on uniformity of valuation. The discussion is based on the assessment of each method for clarity purpose.
Table 1: Sections of the Kwara State and Oyo State Rating Law on Input Variable.

<table>
<thead>
<tr>
<th>S/NO</th>
<th>Variables</th>
<th>Kwara State</th>
<th>Oyo State</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Comparable rent</td>
<td>Section 9 (2) An appraiser may call upon any person liable to pay rate upon a tenement to exhibit to him any accounts, receipts for rent, rent books, or other documents required in connection with valuation of a hereditaments. Section 18 (1) For the purpose of this Law all properties in the State shall be valued by reference to the gross value.</td>
<td>Section 24 (1) An appraiser shall, in determining the gross value, take cognizance of either the actual rent passing on the tenement or of the rent of comparable tenement within the vicinity which has been analysed by him.</td>
<td>The determination of this input is at the discretion of the valuers in the two states. This will be based on the skill on market analysis having obtained necessary data in the respect. So there may be non-uniformity in assessment.</td>
</tr>
<tr>
<td>2</td>
<td>Outgoing</td>
<td>Section 18 (2) The rateable value shall be arrived at by deducting an amount from the gross value; such an amount shall reflect the usual outgoings such as repairs, insurance and management that will be incurred to earn the gross value.</td>
<td>Section 23 (2) The rateable value shall be arrived at by deducting 25% from the value of the tenement value.</td>
<td>There will be uniformity in outgoing rate in Oyo State than Kwara State, as the law is precise on it.</td>
</tr>
<tr>
<td>3</td>
<td>Cost per square meters</td>
<td>Section 20 (1) Before arriving at the depreciated replacement cost of a tenement an appraiser shall: (a) determine the current replacement cost for the tenement including land value.</td>
<td>No provision for this.</td>
<td>This parameter may cause variation in valuation in the two States.</td>
</tr>
<tr>
<td>4</td>
<td>Depreciation rate</td>
<td>Section 20 (1) (b) deduct an amount from the current replacement cost, to allow for age and obsolescence. Section 20(2) the appraiser shall rely on his experience and judgement in determining the amount to be deducted.</td>
<td>Section 25 (1) (b) deduct between 25 per cent and 50 percent from the current replacement cost to arrive at its depreciated replacement cost.</td>
<td>There will be less variation in the valuation in Oyo State than Kwara State as the law is precise on it.</td>
</tr>
<tr>
<td>5</td>
<td>Decapitalisation rate</td>
<td>Section 20 (3) To arrive at the gross value the resultant depreciated replacement cost shall be devalued. The figure arrived at shall be treated in the manner prescribed in subsection (2) of section 18, to arrive at the rateable value</td>
<td>Section 26 the gross value shall (1) be between 8 ½ percent and 10 percent of the depreciated replacement cost, for a commercial tenement; (2) be between 3 ½ percent and 7 ½ percent of the depreciated replacement cost, for a residential tenement;</td>
<td>This input variable will brings some for of uniformity and less variation in Oyo State. The reverse may be the case in Kwara State.</td>
</tr>
<tr>
<td>6</td>
<td>Land value</td>
<td>Section 20 (1) (a). Same as ‘3’ above.</td>
<td>No provision for this</td>
<td>This variable may cause variation in valuation in the two States as there may not uniformity in it adoption.</td>
</tr>
</tbody>
</table>
Divisible balance (book of records) | Section 2, “profit method” means the adjustment of the gross profit to the net profit and applying a figure to the net profit to arrive at the rent to be paid to the landlord. And section 9 (2) quoted above. | Section 12 (b) The rating valuation coordinator may call upon any person liable to pay rate upon a tenement to exhibit to him any accounts, receipts for rent, rent books, or other documents required in connection with valuation of a hereditament. | There may be non-uniformity in this variable in the two States among valuers, as there are about 5 methods of determining this.

| Tenant share methods | Same provision as in ‘7’ above part one | Same provision as in ‘7’ above | ditto |

5.1 The Input Variables in the Comparison Method

The law has stipulated that the gross rent can be sourced from either the rent actually paid, or from a comparable that needs some adjustments. Also, the use of return form is recognized by the two laws. The option left for the appraiser in determining the gross rent are to consult with other firms, adjust the old rental evidence with inflation rate, or analyse the current rent paid with similar property (Ayedun, 2009). These options often lead to non-uniformity in the use of this variable in Nigeria, since the property market lacks reliable data bank or central pool.

The second variable, that is, the outgoing rate, is at the discretion of the judgment or intuition of the appraiser in the case of Kwara State rating law (section 18 subsection 2) whereas, this is expressly stated in section 23(2) of the Oyo State rating law. Twenty-five percent of the gross rent is set aside for outgoing. The practice in Oyo State is similar to the UK practice of ‘statutory deductions to convert gross value to rateable value’ (Ranyer, 1978). ‘Personal opinion or subjective judgment is to be used in determining the rent from the two laws.

The deduction that can be made here is that the valuation will be uniform to some extent in Oyo State whereas, in Kwara State, there would not be uniformity in the outgoing rate. As regard the gross rent as an input variable, there may be no uniformity in the adopted gross rent in the two states.

5.2 The Input Variables in the Depreciated Replacement Cost Method

In this method, the input variables that draw one’s attention to the issue of uniformity of valuation are many. The discussion here on the outgoings is the same to the comparison method that have been discussed above. Other variables are depreciation, cost per square meter, land value, and decapitalisation rate. The decapitalisation rate is usually a statutory rate in property rating practice (Butler et al., 1990; Bond et al., 2011; Leima et al., 2014). This was provided for in the statute in Oyo State (in section 26, decapitalisation rate of between three and a half percent to a maximum of 10% for determining the gross rateable value from the DRC), whereas, no such provision is made in Kwara State rating law. Also, section 25(b) of the Oyo State law prescribes the depreciation method and rate. This is similar to the practice in Tanzania, but contrary to the case in Kwara State. The States laws however, do not either expressly specify or give the responsibility of determining the cost per square meter and land value to any Statutory Officer. This contradicts the practice in Tanzania and Botswana, where the cost per square meter is stated in the tone of the list. Also, the practice of land value in Botswana is not applicable in this two States.

The deduction that can be made here is that there will be uniformity in three input variables out of the five input variables that are required in DRC in Oyo State, whereas, in Kwara State, there may not be uniformity in any of the input variables.
5.3 The Input Variables in the Profit Method

The input variables in the profit method are the outgoings, divisible balance, and the tenant share. The explanation given on outgoings on the other methods is sufficient for the profit method too. The major challenge of this method with respect to uniformity of valuation is in the determination of tenant share. Brown (2013), has identified four ways of determining the tenant’s share, whereas, Bond et al. (2011) suggest five ways. None of the method that can be used in arriving at the tenant share is stated in the two laws. Also, how to determine the divisible balance is not stated in the law.

The two rating laws under exploration do not make specific provisions for the divisible balance and the tenant. With the divergent ways of determining the tenant share, which is a key factor in arriving at the gross rent, and the porosity in the book of record, it is very certain that when valuers value the same hereditament, they will adopt different approaches of tenant share and the likely divisible balance. This however, will lead to non-uniformity of valuation.

From the discussion so far, the input variables have been diagnosed within the provisions of the rating laws in the study area, and the literature on the use of these methods. The input variables in the three methods of valuation for the two States’, which may affect uniformity of valuation are depicted in Figure 1 and 2, but this however, shows that Kwara State rating law identify those input variables, and the responsibility of the tone of the list is given to the appraiser (Consultant Valuer), thus making it a ‘one-man affair’. On the other hand, Oyo State statute specified three of the institutional variables such as depreciation rate, decapitalisation rate and outgoing rate, but the information on how to get other input variables may not guarantee uniformity of valuation, among valuers.

6.0 CONCLUSION

The above discussion has identified the input variables that may influence uniformity of valuation and the position of the law in that regard. The input variables that may influence the uniformity of valuation are the variables that the statutes have failed to make provision for. The input variables that will not ensure uniformity of valuation are more prominent in Kwara State than in Oyo State. This suggests that the rating law in the southern Nigeria may be more comprehensive than that of the Northern Nigeria with respect to the specification of input variables. The direct implication of this is the possibility of non-uniformity in rating valuation in the study areas. The indirect implication may include lengthy time in determining objection and appeal cases, because there is no tone of the list that can be referred to for immediate determination of cases.
This may subsequently lead to higher rate of tax evasion and avoidance, unrest and protests, which lead to low revenue yield (Kuye, 2003; Burg, 2004; Cords, 2006; Babawale and Nubi, 2011; Atilola, 2013).

This paper is recommending that the rating authorities should make the relevant amendments to some of the section that is not clear through their Houses of Assembly. More so, the Rating Boards or Valuation Coordinator in each State should standardise some of the input variables, so that there will be uniformity of valuation. The suggestions offered in this paper if adopted, may reduce the variation in value among valuers when carrying out rating valuation. This approach may ultimately help to enlist the states among nation engaged in best valuation practices in the world. In addition, other States in Nigeria that have taken a cue from the Kwara State and Oyo State property rating laws should also seek appropriate amendments to their laws.

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