

VARIOUS PURPOSES OF VALUATION

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PURPOSES OF VALUATION

In real properties, there are various purposes for which valuation may be required. It is essential to know exactly for what purpose the valuation is being prepared. Valuation is an art and professionals have to consider all pros and cons of the various factors affecting valuation. Broadly speaking, valuation may be required to be done for the following purposes.

- **Use of Valuation Reports in the Sale of Property**

- If the owner of any property wishes to offer the same for sale, it is necessary first and foremost to find out what it would fetch him in monetary terms. Then only can he make a realistic decision on whether to accept or reject an offered price.
- When manufactured articles such as foodgrains, etc. are offered in the market their price can easily be ascertained. In this case, a valuer is not required. However, in the case of real estate or in the case of certain other items when identical properties do not exist the services of a valuer become necessary. In many cases large public companies, trusts or even private individuals, in order to protect their own interests, ask for professional help before selling or purchasing a property.

- **Use of Valuation Reports in the Purchase/Sale of Property**

- Unlike, say the machine or foodgrains no two properties are identical. For instance, a ton of wheat may be similar to another ton of wheat if some factors remain the same such as agricultural requirements, locality where grown, etc. However, a square meter of a particular plot is never exactly the same as another square meter of land, even if it is adjacent to it. Therefore, as properties are always different they require an expert opinion when a purchase is made. An independent valuation is always welcome in this case.
- In addition to getting a monetary value or a numerical figure for his property, a prospective purchaser would normally like to get an opinion of other aspects of the property also. This might include age, future expected life, condition of building, etc. in case of a structure. If it is only land then the type of plot of land, its suitability for a particular purpose, its proximity to a transport head, a market, etc. are factors to be considered. Other factors could be zoning laws, municipal approval, liability of property tax, mortgage, etc.

- **Valuation for Central Government Taxation under Direct Tax Laws**
- Valuation of property is required under various direct tax laws administered by the Central Board of Direct Taxes, Ministry of Finance. These include the Wealth Tax Act, Capital Gains Tax, etc. These valuations are normally required to be done under the particular act for a specific purpose as of a specific date.

- **Valuation Reports used for Fixing Rents and for the Purpose of Forecasting Earnings**
- Any property owner would like to receive a return on his investment that is in conformity with return on other investments. If the owner has constructed a building on his land with the purpose of renting it for whatever purpose, he would like to work out the rent. From these rental incomes and expected outgoings he can forecast the earning capacity of his property.

- **Valuation for Insurance Purpose**
- Insurance policies can be made out against fire damage, theft and loss, earthquake, etc. Insured parties normally bring their valuation reports up-to-date at frequent intervals. Correct insurance coverage is necessary. If the property is overinsured, a higher premium is paid unnecessarily. On the other hand if the property is underinsured, then full loss against actual losses cannot be recovered.

- **Valuation under Land Acquisition Act**
- Normally all democratic governments pay ‘just compensation’ for any property that may be acquired for public good. When property is taken for a public project or for public good, compensating the original owner at a fair market price is necessary. In such a case the acquiring authority as well as the owner of the property may employ different and independent valuers in order to determine the amount of compensation. The competent authority hears evidence from both sides and then decides on the compensation.
- In some cases, a government agency may occupy private property for a certain limited period of time. Under such circumstances, rental value of the property has to be fixed.

- **Valuation in Connection with Mortgages**
- Property of various kinds can be pledged as security against loan. The property may be land, a residential house or any other asset. In such cases, a valuation report on the current market value of the property is necessary. Also, the valuer should give an idea of the property forecast, i.e., probable future trends regarding the property. If the property is income producing, the earning capacity of the property should be indicated. This data will allow the lender to set specific targets for repayment of loan and return of capital.
- Many institutional lenders such as banks and state financial corporations are bound by law to have pledged real estate valued and not to lend more than a certain fixed percentage of this valuation.

- **Valuation for Partition of Properties**
- The distribution of property under a family settlement or a will or on dissolution of a partnership between various claimants warrants valuation of the property. Such valuations form the basis of the settlement or they may be used in any legal proceedings.

- **Valuation for Mergers/Take-overs/Acquisition by Companies**
- In case two or more businesses or enterprises come together, it is necessary to place a value on each so that stocks or shares of the new merged corporation can be apportioned between shareholders. Also when properties are exchanged each asset should be valued.

- **Valuation for Liquidation**

- Very often it happens that a Company has become sick or is not operating for any of several reasons. There may be creditors of the Company who have gone to court for affecting liquidation. The court, in turn, may have appointed an 'official liquidator' to liquidate assets and pay off the creditors. The official liquidator will require an inventory of items and the value or minimum price at which the assets are to be sold. Here also valuation will be required for the liquidation proceedings.

- **Valuation for Leasing Properties and Fixing Lessor/Lessee Interests**
- When properties are leased by an owner (lessor), it is necessary to determine the fair market value of the property in monetary terms. Also, since the lessor is likely to ask for a rent together with a premium (a one time lump sum payment) which may or may not be returnable on expiry of lease, the lease terms would first have to be settled. Valuation in such cases would include present value, estimated future life, annual maintenance costs, and rental value of property.

- **Valuation Requirement in Probate Matters**
- The grant of probate, i.e., for the successors to get the property transferred to their name, is a state subject in India. A valuation for this purpose is necessary as all state governments collect stamp duty under their own laws.

- **Valuation Requirements for Calculating Court Fees and for Other Specific Requirements in Court Cases**
- When legal proceedings are started in court for whatever purpose, normally a court stamp fee is to be estimated. For this purpose, if the subject matter happens to be a real estate immovable property, plant & machinery, etc., a valuation may be necessary. Further, sometimes valuation may be required in court cases involving fraud and damage. A situation may arise when one party, may claim that false facts were presented to it. In such cases a valuation may have to be made taking into account the position that actually existed at the time of sale. The difference in sale price and actual valuation may be assessed as monetary loss to the party

- **Valuation for Accounting Purposes (Asset Valuation)**
- Very often, large companies or other organizations revalue their assets and bring up-to-date the 'historical value' in their books of accounts and balance sheet. This concept is popular in western countries and is gaining ground all over the world whereby the concept of 'current cost accounting' has been introduced. In fact, Britain has introduced legislation whereby large companies adopt this new concept of current cost accounting against the traditional historical accounts so that a true picture of the prevailing actual fixed assets can be reflected in the balance sheet. Valuation will frequently have to be done to keep in line with this concept.

- **Valuation Reports to Study Alternate Investment Opportunities and Economic Feasibility**
- Very often an investor is faced with a choice between alternative investments. Again, in each investment proposal there are several questions likely to arise, i.e., the cost of actual acquisition, the market value of the property, the likely return on investment, etc.

Transferable Development Rights:

- **TDR-** Land Acquisition Act, 1894, Sec-126
- **I) Meaning of TDR** – Making available certain amount of additional built up area in lieu of the area relinquished or surrendered by the owner of land, so that he can use extra built up area either himself or transfer it to another in need of extra built up area for an agreed sum of money. / “TDR is a voluntary incentive based program that allows landowners to sell their development rights from their land to a developer or other development rights from their land to a developer or other interested party who then can use these rights to increase the density of development at another designated location”.
- **Purpose** – For public purpose like road widening, parks, play grounds, school etc.

Benefits of TDR –

- 1) Alternative method of land acquisition
- 2) Process of land acquisition act is comparatively lengthy.
- 3) Easy to get land without any litigation.

Development right certificate – (DRC) –

If the owner of any land which is required for road widening for formulation of new road or development of parks, play grounds, civic amenities etc. those proposed in the plan shall be eligible for the award of TDR. Such award will entitle the owner of the land in the form of a development right certificate (DRC), which he may be use it for himself or transfer to any other person.

Valuation for Time Share Property

- Time Share Concept
- Evolved in France
- Providing cheaper hotel accommodation for Regular visiting people/tourist
- Selling hotel room on temporary ownership right basis (or) fixed time period occupancy basis
- Stay for - Specific number of days without paying charges. But food charge has to be paid. Pro Rata Maintenance charges are applicable
- Time share Right - Saleable in the manner to third party
- Time Share ownership
 - Right to occupy **on lease ownership**
 - Part time Ownership
- Lease Ownership
 - Time Share period - Number of years is fixed (Example 20 years)
 - Purchaser gets right to use specific number of days (1 week) in a years for 20 years period
- After 20 years the time share rights reverts back to Developer.
- During the 20 years period, the purchaser (Lessee) can sell his right to third parties.

52 week are classified into

- Max value: Season class – May, June – Maximum charges
- Classic
- Premium Class

Part time ownership

- Temporary ownership for specified period in specified resort hotel
- 52 weeks - 50 ownership – Pro rata Maintenance Repair and Property tax
- UDS also conveyed
- Temporary ownership Rights can be saleable

Valuation of Time Share Rights

- Comparable sale Method
- Rental Income Method

Role of a Valuer

- Advisor
- Giving opinion to his client.
- Fair Market Value and Interest
- To take financial decision
- Advise on change in possible rental and capital value
- For investment suggestion on policy matter, sinking fund
- Land acquisition case - Date of valuation / Date of notification
- Estate management
 - Maximum income and capital value
 - Securing good maintenance
 - Increase or decrease in capital value
 - To check reasonableness of present rent and outgoings.
 - Provisions for reserve for future repairs.
- Must deliver own independent honest and conscious opinion.
- Not a advice tailored to suit what the client desires.

Function of Valuers

1. Site Inspection
2. Collection of Information and Data
 - Interest to be valued
 - Purpose of valuation
 - Date of valuation
3. Study of Property Market
 - Sales instance
 - Rental instance
 - Compare rate of rentals
 - Compare sale price /unit area
 - Genuine of sale instance
 - Year's Purchase
 - ROI yielded
 - Compare ROI with other alternate form of investment

4. Analysis of Sale

- $\frac{\text{Purchase price(including block money)}}{\text{Net Annual Income}} = YP$
- Remunerative Rate of Interest- Perpetual income
- Accumulative Rate of Interest – Terminable income

5. Estimating Fair Rent

- Property to be Valued Vs. Property involved in the genuine instance of sale

6. Weightage Scene System

- i. Weightage comparison factors
- ii. Land
- iii. Location with amenities and facilities
- iv. Building
- v. Utility services
- vi. Legal
- vii. Economic
- viii. Social

Appropriate weightage is assigned TWS (Total Weightage Scene)

7. Capital Value

- Block and white money

8. Rate of interest

- Yield is 4 to 5 % - Residential property
- Yield is 6 to 10 % - Commercial property

9. Economic condition

- Compare with rate of interest yield with various economic indices like BSE, NITFY, State and Central Government securities, internal rates on lending by banks, inflation rate and Foreign Exchange Rates

10. Capital Appreciation and Capital Erosion

11. Economic Factors

Value of the property subject to

- Physical factors
- Change in legislation
- Change in government policies
- Economic factors
 - Gross domestic Production (GDP)
 - Per capital income
 - Domestic savings
 - Investment in domestic savings in FD, Gold and SB

Duties of Valuer

1. Duty to the Client
2. Duty to the profession of Valuers
3. Duty to the Societies

Duty to the Client

- Reasonable care to performing his functions
- And reasonable care in performing as a professional Valuer

Duty to profession

- Perfect integrity
- Full involvement in the subject matter
- No bias in performing job
- Honesty is the best policy
- Own conscious

Professional Ethics

- Professional is a person who converts his training, skill, knowledge, intelligent, etc., into 'Service' which he imparts to the client / customer and in turn earns money in lieu of his service. Eg. Lawyer, Engineer, Doctor, Chartered Accountant and Valuer
- Ethics in a profession:

There should be healthy competition among the fraternity. To maintain healthy environment in the profession all professionals have to follow certain norms of professional ethics and observe certain code of conduct in their behavior .

Ethics in Valuation profession

Value involves in financial matter

Code of conduct prescribed by the institution of Valuers for its members include, among other, the following rules, by following which professional ethics can be practiced by a Valuer.

1. To ensure mutual co-operation amongst members by free interchange of opinion and experience.
2. To endeavor to protect the profession of valuation concerning all categories from misrepresentation and misunderstanding.
3. To express an opinion only when it is founded on adequate knowledge and honest conviction if he is serving as a witness before a court or commission.
4. To hold in regard the professional reputation of other Corporate Members and not to injure directly or indirectly the professional reputation or practice of another Corporate Member.
5. To exercise the restraint in criticizing the work of another Corporate Member

6. To refrain from associating in work with other valuer who does not conform to ethical practice.
7. To refrain from misrepresenting his qualifications to a client or to the profession.
8. To treat all information acquired during the course of the business strictly confidential unless released by the client or demanded by a court of law.
9. To present clearly the consequence to be expected if the professional judgment is overruled by a non-professional adequacy of work.
10. To observe integrity and fair play in the practice of the profession of valuation
11. To refrain from undertaking to review the work of another Corporate Member of the same client except under Government orders and / or with the knowledge of the first Corporate Member
12. To present the information to the Council of the Institution for action if a Corporate Member considers that another Corporate Member is guilty of the unethical, illegal or unfair practice

13. To order his conduct according to the professional standards and customs of country when a Corporate Member is engaged in Valuation work in a country abroad and to adhere as closely as is practicable to the principals of his code.
14. To give unbiased valuation reports conforming to the objective opinion of the property and not to attempt merely to accommodate the interest of the client
15. To steer clear of situations where interest and duty clash
16. To refrain from entertaining a client who either fails to declare that he had not engaged another value for the same valuation work or produce a clearance certificate of non-objection from the Valuer if already engaged.
17. To conduct yourself and the profession in a manner which will not prejudice your professional status or the reputation of the institution
18. To follow this code as amended and or revised from time to time.

Conclusion

To maintain the healthy relationship amongst the professionals and between professional and the client, it is must for every professional to follow the professional code of conduct and maintain certain ethical standards to ensure the smooth functioning of the profession and to reach the highest level of imparting the professional service.

