Compliance of IVS in Bank Valuation

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INTERNATIONAL VALUATION STANDARDS 2020

1.1. INTRODUCTION TO IVS

1.0. Preamble:

The International Valuation Standards Council is an independent, not-for-profit, private sector standards organization incorporated in the United States and with its operational headquarters in London, UK. IVSC develops international technical and ethical standards for valuations on which investors and others rely.

IVS serve as the key guide for valuation professionals globally and will underpin consistency, transparency and confidence in valuations which are key to investment decisions, financial reporting and financial market stability.

The Glossary defines certain terms used in the International Valuation Standards. This Glossary is applicable to the International Valuation Standards and does not attempt to define basic valuation, accounting or finance terms, as valuers are assumed to have an understanding of such terms (see definition of "valuer").The definitions in this glossary are those used by the IVSC within the current version of IVS.

The latest edition of the International Valuation Standards (IVS) 2020, marks an important milestone towards harmonising valuation practice worldwide.

1.1. Glossary: 20.1. Asset or Assets

Asset or Assets

To assist in the readability of the standards and to avoid repetition, the words "*asset*" and "*assets*" refer generally to items that might be subject to a valuation engagement.

Unless otherwise specified in the standard, these terms can be considered to mean "*asset, group of assets, liability, group of liabilities, or group of assets and liabilities*". (IVS page 3)

1.2. GLOSSARY section 20.18. Weight

Section 20.18. The word "weight" refers to the amount of reliance placed on a particular indication of value in reaching a conclusion of value (**eg, when a single method is used, it is afforded 100% weight).**

1.3. GLOSSARY section 20.19. Weighting

Section 20.19. The word “weighting” refers to the process of analysing and reconciling differing indications of values, typically from different methods and/or approaches**. This process does not include the averaging of valuations**

1.4. IVS FRAMEWORK Section 10. Compliance with Standards

Section 10.1. When a statement is made that a valuation will be, or has been, undertaken in accordance with the IVS, it is implicit that the valuation has been prepared in compliance with all relevant standards issued by the IVSC.

1.5. IVS FRAMEWORK Section 40. Objectivity

Section 40.1. The process of valuation requires the valuer to make impartial judgements as to the reliability of inputs and assumptions. **For a valuation to be credible, it is important that those judgements are made in a way that promotes transparency and minimises the influence of any subjective factors on the process.** Judgement used in a valuation must be applied objectively to avoid biased analyses, opinions and conclusions

1.6. IVS FRAMEWORK Section 60. Departures

Section 60.1. A “departure” is a circumstance where specific legislative, regulatory or other authoritative requirements must be followed that differ from some of the requirements within IVS. Departures are mandatory in that a valuer must comply with legislative, regulatory and other authoritative requirements appropriate to the purpose and jurisdiction of the valuation to be in compliance with IVS. A valuer may still state that the valuation was performed in accordance with IVS when there are departures in these circumstances.

Reference: General Standards IVS 104- Bases of value Section 20.4. Valuers are responsible for understanding the regulation, case law and other interpretive guidance related to all bases of value used.

Section 60.2. The requirement to depart from IVS pursuant to legislative, regulatory or other authoritative requirements takes precedence over all other IVS requirements.

Section 60.3. As required by IVS 101 Scope of Work, para 20.3 (n) and IVS 103 Reporting, para 10.2 **the nature of any departures must be identified** (for example, identifying that the valuation was performed in accordance with IVS and local tax regulations).

If there are any departures that significantly affect the nature of the procedures performed, inputs and assumptions used, and/or valuation conclusion(s), a **valuer must also disclose the specific legislative, regulatory or other authoritative requirements and the significant ways in which they differ** from the requirements of IVS
(For example, identifying that the relevant jurisdiction requires the use of only a market approach in a circumstance where IVS would indicate that the income approach should be used).

Section 60.4. Departure deviations from IVS that are not the result of legislative, regulatory or other authoritative requirements are not permitted in valuations performed in accordance with IVS.

1.7. IVS 102 Investigations and Compliance

Section 40. Compliance with Other Standards

Section 40.1. As noted in the IVS Framework, when **statutory, legal, regulatory or other authoritative requirements** must be followed that differ from some of the requirements within IVS, a valuer must follow the statutory, legal, regulatory or other authoritative requirements (called a “departure”). Such a valuation has still been performed in overall compliance with IVS.

Section 40.2. Most other sets of requirements, such as those written by Valuation Professional Organisations, other professional bodies, or firms’ internal policies and procedures, will not contradict IVS and, instead, typically impose additional requirements on valuers. Such standards may be followed in addition to IVS without being seen as departures as long as all of the requirements in IVS are fulfilled.

DEPARTURE MEANING

1. A departure is the act of leaving somewhere.
2. The fact of a person or vehicle, etc. leaving somewhere
3. A change from what is expected, or from what has happened before
4. the act of leaving a place, job, etc., or an occasion when this happens:
5. A departure from usual behaviour is a change in the way you do something:
6. A change in what is usually done or how something is usually done:

Remarks: There can be no departure from the rules.

To accommodate such departures from the standard update practice, we can allow the administrator to instead specify logical update rules that specify the desired behaviour.

Finally, a crucial claim made by the capability approach is that choice-sensitive departures from functioning achievement should, standardly, be allowed.

Notes: The asset physical description and legal description must comply with all Acts, pertaining to this asset like for a land & building asset, the compliance must be in accordance with the statutory, legal, regulatory or other authoritative requirements.

We can deviate from the method of approach for a specific asset based on the specific legal requirement.

CONDITIONS OF DEPARTURES – LEGISLATIVE REQUIREMENTS

❖ **The Indian Easements Act, 1882 -** Any customary right over immovable property by any one may possess irrespective of other immovable property. An easement right legally possible for a right of way for a property, if the easement right with clearly defined boundaries and duly registered only. If the easement right is only for a stipulated time, then the right is having a time period and also conditions. Likewise, for type of usage also. Any time this easement right may be cancelled. (Example: Tandem / Recessed Plots/ Land locked land)

In Indian Easement Act, all types, for limited time or on condition, restrictive of certain rights and license are defined. While valuing a property having an easement right with an unregistered legal document can be treated as a Departure.

❖ **Government Grants Act, 1875 -** Assigning of Government Owned Lands or Barren lands assigned to a person through issue of legal revenue record making him as owner or granting him permission to develop the properties. Sale is prohibited for certain period and may be restricted sale conditions for the certain class or group of people. If licensed for limited time or on condition, restrictive of certain rights,

❖ **Indian Limitations Act, 1963 -** An Act amended the statute of limitations. Laws of Prescription - If a tenant or a trespasser of the property having an adverse possession or holding or enjoyment of the property for more years – minimum 12 years and above will be called as acquisition of ownership by prescription

❖ **Transfer of Property Act, 1882 -** Under 137 Sections of the Transfer of Property Act, set of definitions have been elaborated for Transfer of Movable and Immovable Properties.

❖ Definition of rights and interests of Mortgagor and Mortgagee, buyer and seller in sale, lease, exchange, charge and gift, corporeal and incorporeal ownership, bundle of rights and ownership form

❖ **Laws of Inheritance - Indian Succession Act, 1925, Hindu Succession Act, 1956, as amended in 2015, Muslim Personal Law (Shariat) Application Act, 1937.**

❖ **Trust Act –** Dealing in trust properties

❖ Minor means any person subject to the **Indian Majority Act, 1875 (9 of 1875**), and "minority" means the status of any such person;

❖ **Land Acquisition Act, 1894 & The Right to Fair Compensation and Transparency in the Land Acquisition, Rehabilitation and Resettlement, Act 2013 (LARAR) -** Acquisition of land for road widening or for public purpose

❖ **Real Estate (Regulation & Development) Act, 2016 (RERA Act**),

❖ **Slum Areas (Improvement and Clearance) Act 1956,**

❖ **Environment (Protection) Act 1986**

❖ **Forest (Conservation) Act of 1980**

CONDITIONS OF DEPARTURES - REGULATORY OR OTHER AUTHORITATIVE REQUIREMENTS

❖ **Special Economic Zones Act, 2005 -** for the promotion of exports

❖ **Factories Act, 1978 -** regulating labour in factories.

❖ **National Highway Act –** Subject to LARAR Act - No Construction Zone

❖ **Railways Act -** No Construction Zone

❖ **Civil Aviation Authority** - No Construction Zone & height restriction in flight path Zone

❖ **Indian Electricity Act** regulates the development of land under power transmission lines. No plot can be developed under if an HT power line transmission passing. A safety distance has to be maintained on either side of the HT power line transmission.

❖ **On Petroleum sale Outlet:** Petroleum Act, Essential Commodity Act, Consumer Protection Act, Explosive Act and restriction on land reconversion

❖ **Coastal Regulation Zone** restrict development on all lands falling 500 metres distance from high tide level

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❖ **Water bodies Regulation:** Sometimes necessary clearance to be sought for properties near irrigation channels, water bodies, rivers.

❖ **Hill Conservation Regulations**: In hilly areas, restriction towards minimum land area of 20 cents in some areas, height restrictions, FSI regulations and land use etc.

❖ **The National Building Code of India (NBC) & IS code of practice,**

❖ **Municipal Law & Town Planning Act & Building bylaws:** Planning Area / Non-planning Area, Land Classification, Approved / unapproved plots, near cemetery / burial ground / cremation, setback areas,

The current use of the land at future date may be changed due to town planning rules. Near to Government banned lands like Mines & Quarries. Municipal Law - Non- Payment of property taxes, height restriction in Heritage towns, the building byelaws or development control rules affect the market value. Important provisions are floor space index, open space rules and height restrictions

❖ For **larger plots open space reservation** is a must. The usable area for development is restricted towards OSR. The current use of the land at future date may be changed due to town planning rules.

❖ **Contemplation of conversion of land use** at a future date will have a say on the market value.

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GENERAL STANDARDS

1.2. IVS 104 BASES OF VALUE

1.0. Value Definition

1.1. Fair Value

Fair value can be referred to the **actual worth of an asset** that will be derived fundamentally by using mathematical methods like DCF, NPV etc., and cannot be determined by any of the factors of market forces.

Fair value is most commonly used in income generating assets like stock markets, etc., instead of any another valuation method. There will be an accuracy in asset valuation.

It will reflect measure of the method utilized.

The fair value mostly remains the same and it will not fluctuate more frequently when one compares fair value to market value.

Fair value is a globally accepted measure and is accepted to International Standards.

2.0. Ind AS 113 – Fair Value:

Measurement defines Fair Value as:

The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Key aspects of Fair Value as per Ind AS 113 include:

(a) **Fair Value is based on the exit price** i.e. the price that would be received to sell an asset or paid to transfer a liability, **not the transaction price or entry price or the price that was actually paid** for the asset or that was received to assume the liability.

Generally, entry and exit prices are different. The idea of exit price is based on expectations about the sale or transfer price from the perspective of market participants as of the valuation date.

Example: A 200 square feet of a shop is for sale. The owner wants to sell it for Rs 70 lakhs. Ongoing market value is Rs 58 lakhs. The shop is rented for the last 30 years and the tenant is presently paying an annual rent of Rs 2,00,000 /- after periodical increase. The present market rent is Rs 3,00,000 /- per annum.

Solution:

1. The exit price on sale price from the buyer as of the valuation date @ 5% on the contract rent will be Rs 40 lakhs and @ 5% on the market rent will be Rs 60 lakhs.

2. The buyer has to spend an amount in vacating the existing tenant. So, Rs 40 lakhs will be ideal and will be the entry price for the buyer.
3. If the seller sells the property @ Rs 60 lakhs, it will be the exit price for the seller.

(b) Ind AS 113, specifies that in the absence of a principal market, the most advantageous market should be considered.
The most advantageous market is the market that maximizes the amount that would be received to sell a given asset or minimizes the amount that would be paid to transfer the liability, after taking into account transaction costs and transportation costs.

(c) Fair Value measurements should reflect market participant assumptions in pricing an asset or liability. Market participants are assumed to be buyers and sellers in the principal (or most advantageous) market that are knowledgeable independent, unrelated parties willing and able to transact for the asset or liability being Fair Valued without compulsion.

(d) The highest and best use ("HABU") of a nonfinancial asset or group of nonfinancial assets and nonfinancial liabilities is the use by market participants that maximizes the value of the nonfinancial assets/liabilities. This Fair Value concept considers
(i) the different ways of utilizing the individual asset/liability, i.e. the highest and best use,
(ii) the valuation premise, whether the maximum value is on a standalone basis or in combination with other assets.

(e) Fair Value measurements should consider characteristics of the assets / liabilities being valued such as the condition, location, restrictions associated with the sale or use of an asset as applicable. Liability fair valuations should reflect non-performance risk.

2.3. IVS Section 90 IFRS 13 Other Basis of Value – Fair Value (International Financial Reporting Standards) –
Section 90.1. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price).
Remarks: The valuer has to value the asset with exit price only and not entry price.

2.3.1. EXAMPLE 1

1. Two similar shops of 2000 square feet are owned by a single owner
2. In one shop, owner himself runs his business and the second one tenanted.
3. Owner occupied shop was sold @ Rs 680 lakhs (34000 per sqft) three months back.
4. The owner wants to sell the second shop for Rs 750 lakhs (37500 per sqft).
5. This shop is rented for the last 20 years and the tenant is presently paying an annual rent of Rs 25,00,000 /- after periodical increase.
6. Further rental agreement for 10 years (Not registered).
7. The present market rent is Rs 35,00,000 /- per annum.

Questions

1. Assuming, the rate of return is 5% what will be capitalized value?
2. Whether to certify the market value Rs 680 lakhs or capitalized value?
3. Can we certify – market rent or contract rent?

Solution

1. The possibility of the sale price as on the valuation date may be either

a) @ 5% on the contract rent of Rs 500 lakhs (Rs 25.00 lakhs / 0.05) or

b) @ 5% on the market rent of Rs 700 lakhs. (Rs 35.00 lakhs / 0.05)

2. **Entry Price**: For the buyer, Rs 500 lakhs will be ideal with the current contract rent and if he buys @ Rs 500 lakhs that will be the entry price for the buyer.

3**. Exit Price:** The seller has to incur a goodwill amount in vacating the existing tenant. If the seller sells the property @ Rs 500 lakhs and adding the Goodwill paid to vacate the tenant, it will be the exit price for the seller

EXAMPLE 2 - The Investment or Income Capitalization Method & HABU

A vacant land of 7500 square feet was bought in the central business district for a consideration of Rs 11.25 crores **last year** @ Rs 1500 per sqft. What will be price that can be offered by a buyer for this vacant land?

Solution:

By Market Approach (Derived from market forces) on the date of valuation.

Current Prevailing Market Rate @ Rs 2,000 per sqft = 7500 sqft x Rs Rs 2000 per sqft

Value of the property by market approach = Rs 15.00 Crs

Based on Market Value, by income approach - Assumptions

Vacant Land of 7500 square feet in CBD. FSI permissible – 2.00. Building area that can be constructed by adopting Hypothetical building scheme is 15000 sq ft (HABU).

Prevailing market rent in the nearby area for shop is Rs 60 /- per sq ft P.M.

GMR receivable PA

= 7500 x 2 FSI x Rs 60/- per sqft x 12 months	= Rs 1.08 crore
Deduct: 10% on outgoes, the NMR	= Rs 0.11crore
Capitalizing Rs 97 lakhs@ 5% on NMR, Value	= Rs 19.40 Crores
Deduction: Proposed Building Construction Cost	
= 15000 sqft x Rs 2,000	= Rs 3.00 Crores
Vacant Land Value =Rs 19.40 Cr - Rs 3.00 Cr	= Rs 16.40 Crs
(Fair Value / Exit price)	**= Rs 16.40 Crs**
	(Actual worth of the vacant land)
(Fair Value / Entry price)	**= Rs 15.00 Cr**
	(Market value of the vacant land)

3.0. Market Value Definition

Market value can be solely determined by the market forces of the factors like economic factors demand and supply, physical factors like location, shape, etc., legal factors and social factors. The valuer has to estimate the amount assuming, as

- ✓ Hypothetical buyer or hypothetical seller and both buyer and seller willing to transact.
- ✓ Both buyer and seller must be knowledgeable.
- ✓ Role of man of ordinary prudence and not super intelligent person or speculator.
- ✓ Market should be open market.

3.1. IVS-Defined Basis of Value – Market Value Section 30

Section 30.1. Market Value is the estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.

Not much difference between the words 'market value' and 'fair market value'. The reported value by the valuer will be on full scrutiny of the documents, physical inspection. It will be

based on after scrutiny of relevant facts, and circumstances that have effect on the value on various aspects like acts and prevailing market conditions.

Fair Market Value may match with market value but it will have rejections on:

- ✓ Distress sale or forced sale transaction that could have occurred
- ✓ Transaction sale between relatives and friends at a concessional price
- ✓ Transaction sales consideration by speculators or purchasers
- ✓ Special purpose to pay fancy price

Notes: Market Value

For the Market value, the influences of distress sale or forced sale transaction, transaction sale between relatives and friends at a concessional price, transaction sales consideration by speculators or purchasers, special purpose to pay fancy price and other bases of value will be deliberated which support of the supply & demand, social, economic, physical and legal factors.

Market value of the asset is not used as commonly valuation method by most of the companies due to its loopholes, limitations and shortcomings. Market value can be determined by demand supply which the market forces and often it will fluctuate more. Market value generally not used and accepted globally.

Fair market Value

But, the Fair market Value has to be determined for a specific asset and this value need not be the same for the adjacent asset. The fair market value has to be adjusted for various terms and conditions based on the specific asset. It is the value that is through fundamental determination. As in the fair value, there will be accuracy in the valuation of an asset and will reflect a true measure of the method.

Fair Value vs Market Value – A Comparison		
	Fair Value	**Market Value**
Definition	Fair Value is referred to the actual worth of an asset	Market Value is the estimated amount of an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.

Derivation of value	Value of an asset is derived fundamentally by using mathematical methods - DCF method. This Fair Value cannot be determined by any of the factors of the market forces.	Market value can be solely determined by the market forces or the factors of the supply and demand. It is the value determined by Social, economic, legal and physical factors
Commonly used	Fair value is the most commonly used in the stock market instead of any another valuation method.	Most of the companies will not commonly use Market valuation method.
Accuracy	As in the fair value, there will be accuracy in the valuation of an asset and will reflect a true measure of the method.	The same is not used by them due to its lacunas, limitations, and shortcomings.
Price Consistency	The fair value of an asset mostly remains constant. It will not vary more often when one compares the former to the market value.	Market value can be determined by the demand and the supply which are the market forces. The same often tends to fluctuate more.
Global acceptance	Fair value is globally acceptable measure - international standards like the IFRS and others.	Market Value is a kind of valuation method which is generally not frequently used. It is not accepted globally.

4.0. IVS Value Definition – Other Basis of Value

Section 40. IVS-Defined Basis of Value – Market Rent

Section 40.1. Market Rent is the estimated amount for which an interest in real property should be leased on the valuation date between a willing lessor and a willing lessee on appropriate lease terms in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.

Section 40.2. Market Rent may be used as a basis of value when valuing a lease or an interest created by a lease. In such cases, it is necessary to consider the contract rent and, where it is different, the market rent.

Section 40.4. Contract Rent is the rent payable under the terms of an actual lease. It may be fixed for the duration of the lease, or variable. The frequency and basis of calculating variations in the rent will be set out in the lease and must be identified and understood in order to establish the total benefits accruing to the lessor and the liability of the lessee.

Section 40.5. In some circumstances the Market Rent may have to be assessed based on terms of an existing lease (eg, for rental determination purposes where the lease terms are existing and therefore not to be assumed as part of a **notional lease).**

Example: A 50 years old tenanted shop of 150 square feet (land & Building) located in the central business district was rented out for Rs 18000/- P.M (**Contract Rent**).
The prevailing market rent in nearby area is Rs 36,000/- P.M **(Market Rent).**
If the valuer assumes, say Rs 25,000/- P.M. for derivation, this rent will be considered as **Notional Rent.**

Section 40.6. In calculating Market Rent, the valuer must consider the following:
(a) in regard to a Market Rent subject to a lease, the terms and conditions of that lease are the appropriate lease terms **unless those terms and conditions are illegal or contrary to overarching legislation**, and
(b) In regard to a Market Rent that is not subject to a lease, the assumed terms and conditions are the terms of a notional lease that would typically be agreed in a market for the type of property on the valuation date between market participants**. (Example: Rental agreement or unregistered lease agreement)**

Section 60. IVS-Defined Basis of Value – Investment Value/Worth

Section 60.1. Investment Value is the value of an asset to a particular owner or prospective owner for individual investment or operational objectives.

Section 60.2. Investment Value is an entity-specific basis (**Section 180**) of value. Although the value of an asset to the owner may be the same as the amount that could be realized from its sale to another party, this basis of value reflects the benefits received by an entity from holding the asset and, therefore, does not involve a presumed exchange. Investment Value reflects the circumstances and financial objectives of the entity for which the valuation is being produced. It is often used for measuring investment performance.

Section 70. IVS-Defined Basis of Value – Synergistic Value

Section 70.1. Synergistic Value is the result of a combination of two or more assets or interests where the combined value is more than the sum of the separate values. If the synergies are only available to one specific buyer then Synergistic Value will differ from Market Value, as the Synergistic Value will reflect particular attributes of an asset that are only of value to a specific purchaser. The added value above the aggregate of the respective interests is often referred to as **"marriage value."**

Section 80. IVS-Defined Basis of Value – Liquidation Value

Section 80.1. Liquidation Value is the amount that would be realized when an asset or group of assets are sold on a piecemeal basis.

Liquidation Value should take into account the costs of getting the assets into saleable condition as well as those of the disposal activity. Liquidation Value can be determined under two different premises of value:

(a) an orderly transaction with a typical marketing period (section 160), or

(b) A forced transaction with a shortened marketing period (section 170).

Section 80.2. A valuer must disclose which premise of value is assumed.

Section 130. Premise of Value/Assumed Use

Section 130.1. A Premise of Value or Assumed Use describes the circumstances of how an asset or liability is used.

Different bases of value may require a particular Premise of Value or allow the consideration of multiple Premises of Value.

Some common Premises of Value are:

(a) Highest and best use **Section 140**,

(b) Current use/existing use **Section 150**,

(c) Orderly liquidation **section 160**, and

(d) Forced sale **section 160**.

Section 140.2. The highest and best use must be physically possible, financially feasible, legally allowed and result in the highest value. If different from the current use, the costs to convert an asset to its highest and best use would impact the value.

Section 140.3. The highest and best use for an asset may be its **current or existing use** when it is being used optimally. However, highest and best use may differ from current use or even be an orderly liquidation.

Section 140.4. The highest and best use of an asset valued on **a stand-alone basis** may be different from its highest and best use as part of a group of assets, when its contribution to the overall value of the group must be considered.

Section 140.5. The determination of the highest and best use involves consideration of the following:

(a) To establish whether a use is physically possible, regard will be had to what would be considered reasonable by participants.

(b) To reflect the requirement to be legally permissible, any legal restrictions on the use of the asset, (example) town planning/zoning designations, need to be taken into account as well as the likelihood that these restrictions will change.

(c) The requirement that the use be financially feasible takes into account whether an alternative use that is physically possible and legally permissible will generate sufficient return to a typical participant, after taking into account the costs of conversion to that use, over and above the return on the existing use.

Example 3 - **<u>Purpose is for Valuation on present day for security</u>**

A vacant land of 1500 square feet was bought in the central business district for a consideration of Rs 1.80 crores **last year** @ Rs 12,000/- per sqft. What is the Fair Value on sale of this vacant land?

Solution:

<u>Market Approach (Derived from market forces)</u>

Current Prevailing Market Rate as on the date of valuation.

Prevailing Market Rate 1500 sqft @ Rs 15,000 per sqft = Rs 2.25 crores

<u>Based on Market Value, by income approach - Assumptions</u>

Vacant Land of 1500 square feet in CBD. FSI permissible – 2.00. Building area that can be constructed by adopting Hypothetical building scheme is 3000 sq ft (HABU).

Prevailing market rent in the nearby area for shop is Rs 50 /- per sq ft P.M.

Gross Maintainable Rent receivable PA = 1500 x 2 FSI x Rs 50/- per square feet x 12 months	Rs 18.0 lakhs
Deduct: 10% on outgoes	(-) Rs 1.80 lakhs
Net Maintainable Rent receivable PA	Rs 16.20 lakhs
Capitalising @ 5% on NMR, Capitalised Value	Rs 324 lakhs
Deduction: Proposed Building Construction Cost = 3000 square feet x Rs 2,000 per square feet	(-) Rs 60 lakhs
Vacant Land Value (Rs 324 lakhs - Rs 60 lakhs)	Rs 264 lakhs
Fair Value / Exit price / Actual worth of the vacant land)	Rs 264 lakhs

Section 150.1. Premise of Value – Current Use/Existing Use

Section 150.1. Current use/existing use is the current way an asset, liability, or group of assets and/or liabilities is used. The current use may be, but is not necessarily, also the highest and best use.

Section 160.1. An orderly liquidation describes the value of a group of assets that could be realized in a liquidation sale, given a reasonable period of time to find a purchaser (or purchasers), with the seller being compelled to sell on an as-is, where-is basis.

Section 160.2. The reasonable period of time to find a purchaser (or purchasers) may vary by asset type and market conditions.

Section 170.1. Premise of Value – Forced Sale

Section 170.1. The term “forced sale” is often used in circumstances where a seller is under compulsion to sell and that, as a consequence, a proper marketing period is not possible and buyers may not be able to undertake adequate due diligence. The price that could be obtained in these circumstances will depend upon the nature of the pressure on the seller and the reasons why proper marketing cannot be undertaken. It may also reflect the consequences for the seller of failing to sell within the period available.

A “forced sale” is a description of the situation under which the exchange takes place, not a distinct basis of value. If an indication of the price obtainable under forced sale circumstances is required, it will be necessary to clearly identify the reasons for the constraint

on the seller, including the consequences of failing to sell in the specified period by setting out appropriate assumptions.

Forced sale value can be in various modes:

1. "As is where is basis"
2. By negotiations amongst limited group of buyers or by public auction
3. Utmost urgency and with assumption of unwilling seller
4. Auction sale of non-performing assets by banks

Section 180. Entity-Specific Factors

Section 180.1. For most bases of value, the factors that are specific to a particular buyer or seller and not available to participants generally are excluded from the inputs used in a market-based valuation.

Examples of entity-specific factors that may not be available to participants include:

(a) Additional value or reduction in value derived from the creation of a portfolio of similar assets,

(b) Unique synergies between the asset and other assets owned by the entity,

(c) Legal rights or restrictions applicable only to the entity,

(d) Tax benefits or tax burdens unique to the entity, and

(e) An ability to exploit an asset that is unique to that entity.

Section 180.2. Whether such factors are specific to the entity, or would be available to others in the market generally, is determined on a case-by-case basis.

For example**,** an asset may not normally be transacted as a stand-alone item but as part of a group of assets. Any synergies with related assets would transfer to participants along with the transfer of the group and therefore are not entity specific.

Section 180.3. If the objective of the basis of value used in a valuation is to determine the value to a specific owner (such as Investment Value/Worth discussed in paras 60.1 and 60.2), entity-specific factors are reflected in the valuation of the asset. Situations in which the value to a specific owner may be required include the following examples:

(a) Supporting investment decisions, and

(b) Reviewing the performance of an asset.

Section 190. Synergies

Section 190.1. "Synergies" refer to the benefits associated with combining assets.

When synergies are present, the value of a group of assets and liabilities is greater than the sum of the values of the individual assets and liabilities on a stand-alone basis. Synergies typically relate to a reduction in costs, and/or an increase in revenue, and/or a reduction in risk.

Section 190.2. Whether synergies should be considered in a valuation depends on the basis of value. For most bases of value, only those synergies available to other participants generally will be considered (see discussion of Entity-Specific Factors in paras 180.1-180.3).

Section 190.3. An assessment of whether synergies are available to other participants may be based on the amount of the synergies rather than a specific way to achieve that synergy.

Section 200. Assumptions and Special Assumptions

Section 200.1. In addition to stating the basis of value, it is often necessary to make an assumption or multiple assumptions to clarify either the state of the asset in the hypothetical exchange or the circumstances under which the asset is assumed to be exchanged. Such assumptions can have a significant impact on value.

Section 200.4. Where assumed facts differ from those existing at the date of valuation, it is referred to as a "special assumption". Special assumptions are often used to illustrate the effect of possible changes on the value of an asset. They are designated as "special" so as to highlight to a valuation user that the valuation conclusion is contingent upon a change in the current circumstances or that it reflects a view that would not be taken by participants generally on the valuation date. Examples of such assumptions include, without limitation:

(a) An assumption that a **property is freehold with vacant possession**,

(b) An assumption that a proposed **building had actually been completed** on the valuation date,

(c) An assumption that a specific contract was in existence on the valuation date which had not actually been completed, and

Section 200.5. **All assumptions and special assumptions must be reasonable under the circumstances, be supported by evidence, and be relevant having regard to the purpose for which the valuation is required.**

* * *

GENERAL STANDARDS

2. IVS 105 VALUATION APPROACHES AND METHODS

2.1. INCOME APPROACH

Introduction: Marketability of an asset is based on the willing buyer to acquire for reasons like desire, utility, or income generation or an investment or for a specific purpose. Utility of asset involving existing and future benefits due to possession and use of the property is one of the factor.

There must be a demand for the property. If there is a scarcity, then the demand will increase or if it is abundance or supply is more demand will be less. The legal factor of the property is that it must be transferable with a clear perfect title.

Basic property types based on marketability - Marketable and Non-Marketable Properties.

Examples: Income fetching Marketable Properties: Hotels, Cinemas, malls, petrol pumps, industrial properties, leased properties

Examples: Non-income fetching but marketable Properties: Self occupied house, flats, shops, factories, freehold land.

Examples: Non–income fetching and non-marketable Properties: Educational Institutions Temples, Public and Government buildings, Fire station, museum etc.

Methods of valuation varies depending upon the types of properties: For Income fetching Marketable Properties, both market approach and income approach methods can be adopted. For Non-income fetching but marketable properties the method to be adopted is the market approach method. For non-marketable properties either by cost approach or income approach method (if it is an income generation property) has to be followed.

Section 40. Income Approach

Section 40.1. The income approach provides an indication of value by converting future cash flow to a single current value. Under the income approach, the value of an asset is determined by reference to the value of income, cash flow or cost savings generated by the asset.

Section 40.2. The income approach should be applied and afforded significant weight under the following circumstances:

(a) The **income-producing ability** of the asset is the **critical element** affecting value from a participant perspective, and/or

(b) **Reasonable projections** of the amount and **timing of future income** are available for the subject asset, but there are few, if any, relevant market comparable.

Example 1. A client purchased a vacant land of 3000 square feet in the main commercial zone for a consideration of Rs 4.50 crores **two years back. Current Prevailing Market Rate** @ Rs 18,000 per sqft is Rs 5.40 crores as on the date of valuation.
Prevailing market rent in the nearby area for shop per month is Rs 50 / per sqft. FSI permissible in that area is 2.50.
What will be excess amount, if the client use the property on HABU basis for purchase of the property which would match with market rent?

Data & Assumptions	
Vacant Land extent.	3000 sq.ft
FSI permissible – 2.50. Building area that can be constructed	7500 sq ft
Prevailing market rent in the nearby area for shop per month	Rs 50 / sq ft
Purchased cost of the vacant land	Rs 450 lakhs
Prevailing Market Rate 3000 sqft @ Rs 18,000 per sqft	Rs 540 lakhs
Solution:	
GMR receivable PA = 7500 x Rs 50/- per sqft x 12 months	Rs 45.0 lakhs
Deduct: 10% on outgoes	- Rs 4.50 lakhs
Net maintainable rent (NMR)	Rs 40.50 lakhs
Capitalising @ 5% on NMR, Capitalised Value including building	Rs 810 lakhs
Deduction: Proposed Building Construction Cost = 7500 sqft x Rs 2,500 per sqft	(-)Rs 188 lakhs
Vacant Land Value **(Fair Value / Actual Worth)** Rs 810 lakhs - Rs 188 lakhs	Rs 622 lakhs
Vacant land value as per Market value basis	Rs 540 lakhs
Difference between Fair value and Market value	Rs 82 lakhs

Section 40.3. Although the above circumstances would indicate that the income approach should be applied and afforded significant weight, the following are additional circumstances where the income approach may be applied and afforded significant weight.

When using the income approach under the following circumstances, a valuer should **consider whether any other approaches can be applied** and weighted to corroborate the value indication from the income approach**:**

(a) The **income-producing ability** of the subject asset is only one of several factors affecting value from a participant perspective,

(b) There is **significant uncertainty** regarding the amount and **timing of future income**-related to the subject asset,

(c) There is a **lack of access to information** related to the subject asset (for example, a minority owner may have access to historical financial statements but not forecasts/budgets),

(d) Subject **asset has not yet begun generating income**, but is projected to do so.

Section 40.4. A fundamental basis for the income approach is that investors expect to receive a return on their investments and that such a return should reflect the perceived level of risk in the investment.

Section 40.5. Generally, investors can only expect to be compensated for systematic risk (also known as “market risk” or “un-diversifiable risk”).

Notes: There are many main investment types, or asset classes, that you can choose from, each with distinct characteristics, risks and benefits.

- Growth investments.
- Shares
- Property.
- Defensive investments
- Cash
- Fixed interest.

There are many ways to categorize a company's financial risks. One approach for this is provided by separating financial risk into four broad categories:

- Market risk
- Credit risk
- Liquidity risk
- Operational risk

Within the risks types, there are certain specific types of risk, which every investor must know. Credit Risk (also known as Default Risk). The discount rate depends upon the risk factor, specific to each and every asset and also on the basic requirement of the investor.

- Country Risk
- Political Risk
- Reinvestment Risk
- Interest Rate Risk
- Foreign Exchange Risk
- Inflationary Risk
- Market Risk

Section 50. Income Approach Methods

Section 50.1. Although there are many ways to implement the income approach, methods under the income approach are effectively based on discounting future amounts of cash flow to present value.

They are variations of the Discounted Cash Flow (DCF) method and the concepts below apply in part or in full to all income approach methods.

Discounted Cash Flow (DCF) Method

Section 50.2. Under the DCF method the forecasted cash flow is discounted back to the valuation date, resulting in a present value of the asset.

Section 50.3. In some circumstances for long-lived or indefinite-lived assets, DCF may include a terminal value which represents the value of the asset at the end of the explicit projection period. In other circumstances, the value of an asset may be calculated solely using a terminal value with no explicit projection period. This is sometimes referred to as an income capitalization method.

Section 50.4. The key steps in the DCF method are:

(a) Choose the **most appropriate type of cash flow** for the nature of the subject asset and the assignment (i.e. pre-tax or post-tax, total cash flows or cash flows to equity, real or nominal, etc.),

(b) Determine the most **appropriate explicit period**, if any, over which the cash flow will be forecast,

(c) Prepare **cash flow forecasts** for that period,

(d) Determine whether a **terminal value** is appropriate for the subject asset at the end of the explicit forecast period (if any) and then determine the appropriate terminal value for the nature of the asset,

(e) Determine the **appropriate discount rate**, and

(f) **Apply the discount rate to the forecasted future cash flow, including the terminal value**, if any.

Type of Cash Flow

Section 50.5. When selecting the appropriate type of cash flow for the nature of asset or assignment, valuers must consider the factors below. In addition, the discount rate and other inputs must be consistent with the type of cash flow chosen.

(a) Cash flow to whole asset or partial interest: Typically, cash flow to the whole asset is used. However, occasionally other levels of income may be used as well, such as cash flow to equity (after payment of interest and principle on debt) or dividends (only the cash flow distributed to equity owners).

Cash flow to the whole asset is most commonly used because an asset should theoretically have a single value that is independent of how it is financed or whether income is paid as dividends or reinvested.

(b) The cash flow can be pre-tax or post-tax: the tax rate applied should be consistent with the basis of value and in many instances would be a participant tax rate rather than an owner-specific one.

(c) Nominal versus real cash flow does not consider inflation whereas nominal cash flows include expectations regarding inflation. If expected cash flow incorporates an expected inflation rate, the discount rate has to include an adjustment for inflation as well.

(d) Currency: The choice of currency used may have an impact on assumptions related to inflation and risk. This is particularly true in emerging markets or in currencies with high inflation rates. The currency in which the forecast is prepared and related risks are separate and distinct from risks associated with the country (ies) in which the asset resides or operates.

(e) The type of cash flow contained in the forecast: For example, a cash flow forecast may represent expected cash flows, ie, probability-weighted scenarios), most likely cash flows, contractual cash flows, etc.

Section 50.6. The type of cash flow chosen should be in accordance with participant's viewpoints. For example, cash flows and discount rates for real property are customarily developed on a pre-tax basis while cash flows and discount rates for businesses are normally developed on a post-tax basis. Adjusting between pre-tax and post-tax rates can be complex and prone to error and should be approached with caution.

Section 50.7. When a valuation is being developed in a currency ("the valuation currency") that differs from the currency used in the cash flow projections ("the functional currency"), a valuer should use one of the following two currency translation methods:
(a) Discount the cash flows in the functional currency using a discount rate appropriate for that functional currency. Convert the present value of the cash flows to the valuation currency at the spot rate on the valuation date.
(b) Use a currency exchange forward curve to translate the functional currency projections into valuation currency projections and discount the projections using a discount rate appropriate for the valuation currency. When a reliable currency exchange forward curve is not available (for example, due to lack of liquidity in the relevant currency exchange markets), it may not be possible to use this method and only the method described in para 50.7(a) can be applied.

Explicit Forecast Period

Section 50.8. The selection criteria will depend upon the purpose of the valuation, the **nature of the asset, the information available and the required bases of value. For an asset with a short life, it is more likely to be both possible and relevant to project cash flow over its entire life.**

Section 50.9. Valuers should consider the following factors when selecting the explicit forecast period:
(a) The **life of the asset**,
(b) A **reasonable period** for which reliable data is available on which to base the projections,
(c) The **minimum explicit forecast period** which should be sufficient for an asset to achieve a stabilized level of growth and profits, after which a terminal value can be used,
(d) In the valuation of cyclical assets, the explicit forecast period should generally include an entire cycle, when possible, and

(e) For finite-lived assets such as most financial instruments, the cash flows will typically be forecast over the full life of the asset.

Example: Though an asset having economic life of 60 years, there is a possibility of the life is reduced to 30 years, due to legal constraints (The lease covenant stipulates that the lessee has to demolish the structure after expiry of lease period and the lessee has to surrender the vacant land to the lessor), the minimum explicit forecast period is to be considered for 30 years for the lessee.

Section 50.10. In some instances, particularly when the asset is operating at a stabilized level of growth and profits at the valuation date, it may not be necessary to consider an explicit forecast period and a terminal value may form the only basis for value (sometimes referred to as an income capitalization method).

Section 50.11. The intended holding period for one investor should not be the only consideration in selecting an explicit forecast period and should not impact the value of an asset. However, the period over which an asset is intended to be held may be considered in determining the explicit forecast period if the objective of the valuation is to determine its investment value.

Notes: In a leased asset, if the lessee is to surrender the asset as and where it is condition, to the lessor, the balance holding period can be taken as the economic life of the asset for the lessor.

In a leased asset, if the lessee is to demolish / remove the asset on the lease expiry, surrender the vacant possession to the lessor, the forecast period can be taken as the leased life (life due to legal constraints) of the asset.

Cash Flow Forecasts

Section 50.12. Cash flow for the explicit forecast period is constructed using **prospective financial information (PFI)** (projected income/inflows and expenditure/outflows).

Section 50.13. As required by para 50.12, regardless of the source of the PFI (eg, management forecast), a valuer must perform analysis to evaluate the PFI, the assumptions underlying the PFI and their appropriateness for the valuation purpose. The suitability of the PFI and the underlying assumptions will depend upon the purpose of the valuation and the required bases of value. For example, cash flow used to determine market value should

reflect PFI that would be anticipated by participants; in contrast, investment value can be measured using cash flow that is based on the reasonable forecasts from the perspective of a particular investor.

Example: Two similar shops are rented out on monthly basis. First shop for a period of 15 years and the second one for 25 years period.

Or it may be, for the first shop with a renewable clause of 10 years with an increase of rent after 15 years and the second one without renewal clause and rent renewal.

In this case, the prospective financial information is different for the perspective of a particular investor

Section 50.14. The cash flow is divided into suitable periodic intervals (eg, weekly, monthly, quarterly or annually) with the choice of interval depending upon the nature of the asset, the pattern of the cash flow, the data available, and the length of the forecast period.

Example: Two similar flats are rented out. The first flat is given on rent for Rs 15000 per month, whereas the second one is let out for Rs 50000 on quarterly basis (3 months). Hence, different types of cash flow must reflect the level of risk and it requires different discount rates.

Section 50.15. The projected cash flow should capture the amount and timing of all future cash inflows and outflows associated with the subject asset from the perspective appropriate to the basis of value.

Section 50.16. Typically, the projected cash flow will reflect one of the following:

(a) Contractual or promised cash flow,

(b) The single most likely set of cash flow,

(c) The probability-weighted expected cash flow, or

(d) Multiple scenarios of possible future cash flow.

Section 50.17. Different types of cash flow often reflect different levels of risk and may require different discount rates.

For example, probability-weighted expected cash flows incorporate expectations regarding all possible outcomes and are not dependent on any particular conditions or events (note that when a probability-weighted expected cash flow is used, it is not always necessary for valuers to take into account distributions of all possible cash flows using complex models and

techniques. Rather, valuers may develop a limited number of discrete scenarios and probabilities that capture the array of possible cash flows).

A single most likely set of cash flows may be conditional on certain future events and therefore could reflect different risks and warrant a different discount rate.

Example: Two similar flats are rented out. The first flat is given on rent for Rs 15000 per month for 5 years period, whereas the second one is let out for Rs 50000 on quarterly basis for 10 years.

The pattern of the cash flow is different for the flats.

The data available (i.e. rental pattern) is different for the flats.

The length of the forecast periods are different for the flats.

May be after 5 years the first flat may be vacant for certain period of time also. Hence, different types of cash flow must reflect the level of risk and it require different discount rates.

Section 50.18. While valuers often receive PFI that reflects accounting income and expenses, it is generally preferable to use cash flow that would be anticipated by participants as the basis for valuations.

For example, accounting non-cash expenses, such as depreciation and amortization, should be added back, and expected cash outflows relating to capital expenditures or to changes in working capital should be deducted in calculating cash flow.

Section 50.19. Valuers must ensure that seasonality and cyclicality in the subject has been appropriately considered in the cash flow forecasts.

Terminal Value

Section 50.20. Where the asset is expected to continue beyond the explicit forecast period, valuers must estimate the value of the asset at the end of that period. The terminal value is then discounted back to the valuation date, normally using the same discount rate as applied to the forecast cash flow.

Section 50.21. The terminal value should consider:

(a) Whether the asset is deteriorating/finite-lived in nature or indefinite-lived, as this will influence the method used to calculate a terminal value,

(b) Whether there is future growth potential for the asset beyond the explicit forecast period,

(c) Whether there is a pre-determined fixed capital amount expected to be received at the end of the explicit forecast period,
(d) The expected risk level of the asset at the time the terminal value is calculated,
(e) For cyclical assets, the terminal value should consider the cyclical nature of the asset and should not be performed in a way that assumes “peak” or “trough” levels of cash flows in perpetuity, and
(f) The tax attributes inherent in the asset at the end of the explicit forecast period (if any) and whether those tax attributes would be expected to continue into perpetuity.

Section 50.22. Valuers may apply any reasonable method for calculating a terminal value. While there are many different approaches to calculating a terminal value, the three most commonly used methods for calculating a terminal value are:
(a) Gordon growth model/constant growth model **(appropriate only for indefinite-lived assets),**
(b) Market approach / exit value **(appropriate for both deteriorating / finite-lived assets and indefinite-lived assets), and**
(c) Salvage value/disposal cost **(appropriate only for deteriorating/ finite-lived assets).**

Market Approach / Exit Value
Section 50.24. The market approach/exit value method can be performed in a number of ways, but the ultimate goal is to calculate the value of the asset at the end of the explicit cash flow forecast.

Section 50.25. Common ways to calculate the terminal value under this method include application of a market-evidence based capitalization factor or a market multiple.

Section 50.26. When a market approach/exit value is used, valuers should comply with the requirements in the market approach and market approach methods section of this standard (sections 20 and 30). However, valuers should also consider the expected market conditions at the end of the explicit forecast period and make adjustments accordingly.
Example: A 50 years old tenanted shop of 150 square feet (land & Building) located in the central business district. The landlord of the shop is offering for sale for Rs 50 lakhs.
The guideline rate is Rs 15000 /-per square foot. Prevailing market rate is Rs 28,000/- per square foot.

It was rented out for Rs 4/- per square foot per day (Rs 18000/- P.M.). The prevailing market rent in nearby area is Rs 8 /-per square foot per day (Rs 36,000/- P.M)

Questions:

1. In case of Recession or any eventuality, PMR will go up or come down?
2. Or the tenant resists to vacate the shop and prevent the seller to sell the shop?
3. Or what will be the offer price by tenant, if the tenant wishes to purchase the shop for himself?

Data	
Sale offer price of the shop @ Rs 33,333/- per sqft for 150 sft	Rs 50.00 lakhs
Guideline rate (GLV) @ Rs 15000 /-per sqft x 150 sqft	Rs 22.50 lakhs.
Present market rate (PMR) @ Rs 28,000/- per sqft x 150 sqft	Rs 42.00 lakhs
Present Market rent	Rs 36000/-PM
Actual contract rent paid by the tenant	Rs 18000/- PM
Shop is tenanted for more than 50 years	
Solution	
Annual Gross rent = Rs 18000 x 12 months	Rs 2,16,000
Less Outgoes @ 10% on Rs 2,16,000	Rs 21,600
Annual Net rent = Rs 2,16,000 - Rs 21,600	Rs 1,94,400
Actual return(i.e.) Capitalised value @ 5% **Present Worth or Exit Value**	Rs 38,88,000
Present Worth per square foot = Rs 38,88,000/150	Rs 25920/- per sqft

Answers:

1. In case of Recession or any eventuality, PMR will come down.
2. If the tenant resists to vacate the shop and prevent the seller to sell the shop, it will be the minimum value of Rs 38.80 lakhs for the seller to exit. **(Exit Price)**
3. And for the buyer, he has to spent additional amount in vacating the tenant as goodwill. So, he will not offer more than 38.88 lakhs. **(Entry Price)**

38.88 lakhs will be the offer price by tenant, if the tenant wishes to purchase the shop for himself

Salvage Value/Disposal Cost

Section 50.27. The terminal value of some assets may have little or no relationship to the preceding cash flow. **Examples of such assets include wasting assets such as a mine or an oil well.**

Section 50.28. In such cases, the terminal value is typically calculated as the salvage value of the asset, less costs to dispose of the asset.

In circumstances where the costs exceed the salvage value, the terminal value is negative and referred to as a disposal cost or an asset retirement obligation.

Discount Rate

Section 50.29. The rate at which the forecast cash flow is discounted should reflect not only the time value of money, but also the risks associated with the type of cash flow and the future operations of the asset.

Section 50.30. The discount rate **must be consistent** with the type of cash flow.

Section 50.31. Valuers may use any reasonable method for developing an appropriate discount rate.

Notes: Yield is another name for the rate of return. A property's yield, while similar to its capitalization (cap) rate, can differ in that **yield measures income / total cost**, while **cap rate measures income / price or value**.

Generally, yield is calculated by dividing the net operating income or interest received on a set period of time by either the amount originally invested or by its current price.

Yield is defined as the income return on investment. This refers to the net operating income or interest received from a security and is usually expressed as an annual percentage based on the investment's cost, its current market value, or its face value.

The **nominal interest rate** is the interest rate before taking inflation into account, in contrast to real interest rates and effective interest rates.

Example: The nominal interest rate (or money interest rate) is the percentage increase in money you pay the lender for the use of the money you borrowed. For instance, imagine that you borrowed Rs1.00 lakh from your bank one year ago at 8% interest on your loan.

A **real interest rate** is an interest rate that has been adjusted to remove the effects of inflation to reflect the real cost of funds to the borrower and the real yield to the lender or to an investor. The real interest rate reflects the rate of time-preference for current goods over future goods.

The **Fisher equation** provides the link between nominal and real interest rates. To convert from nominal interest rates to real interest rates, we use the following formula:

Real interest rate ≈ nominal interest rate − inflation rate. To find the real interest rate, we take the nominal interest rate and subtract the inflation rate.

Example: if a loan has a 12 percent interest rate and the inflation rate is 8 percent, then the real return on that loan is 4 percent.

Section 50.32. Valuers should consider corroborative analyses when assessing the appropriateness of a discount rate. While there are many methods for developing a discount rate or determining the reasonableness of a discount rate, a non-exhaustive list of common methods includes:

1) The capital asset pricing model (CAPM):
2) The weighted average cost of capital (WACC):
3) The observed or inferred rates/yields:
4) The internal rate of return (IRR):
5) The weighted average return on assets (WARA):
6) Net Present Value Method

(a) **Capital Asset Pricing Model (CAPM**), The Capital Asset Pricing Model (**CAPM**) describes the relationship between systematic risk and expected return for assets, particularly stocks.

CAPM is widely used throughout finance for pricing risky securities and generating expected returns for assets given the risk of those assets and cost of capital.

The capital asset pricing model is a model used to determine a theoretically appropriate required rate of return of an asset, to make decisions about adding assets to a well-diversified portfolio.

Example - A hospitality building of 20505 square feet of land with 38811 square feet of building. The building consists of stilt floor + 4 floors, aged 2 years. The purchased price is Rs 53.00 Crores. This property is leased out to a management for 15 years. The old building is renovated now as per the requirement of the lessee. The lessor has invested an additional

amount Rs 10.00 Crores for renovation purpose. The lessor has totally invested Rs 63.00 Crores in purchasing, renovating to suit the client (lessee). Lease terms as follows:

Lease deed terms:

1. **Total rooms**: 66 (200-220 square feet area)
2. The lease shall be for a period of 15 years commencing from the time of the final agreement is signed
3. **Lock-in period** : 3 years
4. **Lease payment schedule**:

a. Rs 17.00 lakhs for first year

b. Rs 18.00 lakhs for second year

c. Rs 18.00 lakhs for third year

d. **Escalation Clause**: 15% on completion of every 3 years

e. **Refundable deposit:** Rs 140 lakhs

5. **Registration agreement fee:** To be borne by both parties @ 50% each
6. **Grace period to run the hotel:** 75 days after completion and then the rental starts
7. **Exit clause:** 6 months' notice is only with the tenant even after completion of the lock-in period

Basis of Working

Total cost of the project invested by the lessor			₹ 6300,00,000
Maintenance expenses to be borne by			By lessee
Lease period including lock in period of 3 years			15 years
Lessee terms	Lease rent amount per year	interest @ 12% PA Simple interest	Total return
Refundable deposit	140,00,000	16,80,000	156,80,000
First year rent	204,00,000	24,48,000	228,48,000
Second year rent	216,00,000	25,92,000	241,92,000
Third year rent	216,00,000	25,92,000	241,92,000
Fourth year rent	248,40,000	29,80,800	278,20,800
Fifth year rent	248,40,000	29,80,800	278,20,800

Sixth year rent	248,40,000	29,80,800	278,20,800
Seventh year rent	285,66,000	34,27,920	319,93,920
Eighth year rent	285,66,000	34,27,920	319,93,920
Ninth year rent	285,66,000	34,27,920	319,93,920
Tenth year rent	328,50,900	39,42,108	367,93,008
Eleventh year rent	328,50,900	39,42,108	367,93,008
Twelfth year rent	328,50,900	39,42,108	367,93,008
Thirteenth year rent	377,78,535	45,33,424	423,11,959
Fourteenth year rent	377,78,535	45,33,424	423,11,959
Fifteenth year rent	377,78,535	45,33,424	423,11,959
Total income	4497,06,305	539,64,756	5036,71,061
Less deposit	-140,00,000		-140,00,000
Total	4357,06,305	539,64,756	4896,71,061
Less taxes & others	-43570631	-5396476	-48967106
Net income	3921,35,674	485,68,280	4407,03,955
Average net income	261,42,378	32,37,885	293,80,264
Rate of Return	4.15%	0.51%	4.66%

(b) **Weighted Average Cost of Capital (WACC**):

The weighted average cost of capital (WACC) is a calculation of a firm's cost of capital in which each category of capital is proportionately weighted. All sources of capital, including common stock, preferred stock, bonds, and any other long-term debt, are included in a WACC calculation.

The weighted average cost of capital (WACC) is the rate that a company is expected to pay on average to all its security holders to finance its assets. The WACC is commonly referred to as the firm's cost of capital. Importantly, it is dictated by the external market and not by management.

(c) **Observed or Inferred Rates/Yields** - The real interest rate is the rate of interest an investor, saver or lender receives after allowing for inflation.

It can be described more formally by the Fisher equation, which states that the real interest rate is approximately the nominal interest rate minus the inflation rate.

Value indications from other approaches, such as market approach, or comparing implied multiples from the income approach with guideline company market multiples or transaction multiples can also be adopted.

(d) **Build-Up Method**. The Build-Up Method is a widely recognized **method** of determining the after-tax net cash flow discount rate, which in turn yields the capitalization rate. The figures used in the Build-Up Method are derived from various sources.

(e) **Internal rate of return (IRR**)

The internal rate of return is a measure of an investment's rate of return. The term internal refers to the fact that the calculation excludes external factors, such as the risk-free rate, inflation, the cost of capital, or various financial risks.

It is also called the discounted cash flow rate of return.

Internal rate of return (**IRR**) is the interest rate at which the net present value of all the cash flows (both positive and negative) from a project or investment equal zero.

Internal rate of return is used to evaluate the attractiveness of a project or investment.

(f) **Net Present Value Method**

In Net present value approach, all cash flows are discounted using the required rate of return which is minimum an investor requires on the investment.

The discounted rate will be generally be the minimum rate of return required over a period of cash flow. If the total of the discounted cash flow over a period is zero, then it is a good investment.

Multiplication of anticipated future cash flow by discounted rate of return gives the net present value. For this, estimate the net cash flow during the period.

Net Present Value Method has two characteristics. For the assumed net cash flow same discounted rate of return is adopted. NPV will always decreases as the discount rates of return increases. It takes into consideration of the time value of money. The cash flow stream is taken into account in its totality. NPV represents the wealth of the investor in present day money terms after adjusting for return on the investment.

Example - 'A' agrees to sell his property to 'B' for Rs 5.00 lakhs. 'B' agrees to pay in 5 instalments & pay the first payment on date of agreement. The balance In 4 equal Instalments on every 2 Months. The prevailing Rate of Return Is 13.50% P.A.. What is NPV for 'A'?

Internal Rate of Return (IRR)

It is defined as the rate at which discounted flow will match with the initial investment or net present value will be zero. It is the actual rate of return from investment. It takes into account considering all future discounted receipts and discounted payments are equal making NPV zero. IRR can be calculated by trial and error method or by linear interpolation.

Instalment No	Amount Paid	R / Month	No of Period	Discount Rate $\frac{1}{(1+R)^n}$	NPV
1	Rs 1,00,000	0.01125	0	1.00	Rs 1,00,000
2	Rs 1,00,000	0.01125	2	0.977874	Rs 97,787
3	Rs 1,00,000	0.01125	4	0.9562377	Rs 95,624
4	Rs 1,00,000	0.01125	6	0.93508	Rs 93,508
5	Rs 1,00,000	0.01125	8	0.9143905	Rs 91,439
6					Rs 4,78,358

IRR example

A flat purchased in 31.12.1987 for Rs 1.50 lakhs. Owner received rental advance for 2 years of Rs 18000 as the same date. He spent for repairing the flat for Rs 10000 on 31.12.1989. On the same date he received rental advance of Rs 5000 for 1 year for year 1990. Again, he spent Rs 9000 on renovation of the flat on 31.12.1990. On the same day, he received rental advance of Rs 10000 for 2 years for 1991 & 1992. He received rental advance of Rs 6000 for 1 year for 1993. Finally, he sold the flat on 31.12.1993 for Rs 1,90,000. What is the IRR?

Assumption: 1. Rate of return of 7% per annum

Date (p)	Time / years (n)	Cash flow (C) = - Outgoes = + income	R% per annum assumed	Discount Rate $\frac{1}{(1+R)^n}$	Present value = C x D

31.12.1987	0	- Rs 1,32,000	0.07	1	- Rs 1,32,000
31.12.1989	2	- Rs 5,000	0.07	0.8734	- Rs 4367
31.12.1990	3	+ Rs 1,000	0.07	0.8163	+ Rs 816
31.12.1992	5	+ Rs 6,000	0.07	0.7130	+ Rs 4278
31.12.1993	6	+ Rs 1,90,000	0.07	0.6663	+Rs 1,26,597
Net Present Value					- Rs 4676

Assumption: 2. Rate of return of 6% per annum

Date (p)	Time / years (n)	Cash flow (C) = - Outgoes = + income	R% per annum assumed	Discount Rate $\frac{1}{(1+R)^n}$	Present value = C x D
31.12.1987	0	- Rs 1,32,000	0.06	1	- Rs 1,32,000
31.12.1989	2	- Rs 5,000	0.06	0.8900	- Rs 4450
31.12.1990	3	+ Rs 1,000	0.06	0.8396	+ Rs 840
31.12.1992	5	+ Rs 6,000	0.06	0.7473	+ Rs 4484
31.12.1993	6	+ Rs 1,90,000	0.06	0.7050	+Rs 1,33,950
Net Present Value					+ Rs 2824

By linear interpolation method we can find actual IRR by making NPV zero. From this example NPV arrived is (a) + Rs 2824 @ 6% & (b) - Rs 4676 @ 7%. But this must be zero. So, IRR must be between 6% & & 7%. To find the actual IRR, the linear interpolation method is used.

Formula: IRR = R_1 + (R2-R_1) X $\frac{N1}{(N1+N2)}$

IRR = actual rate of return

R_1 = Lower rate of return,

R_2 = higher rate of return

N_1 = Lower net present value,

N_2= Higher net present value

IRR = 6 + (7-6) $\mathcal{X}$ $\frac{2824}{(2824+4676)}$ = 6.3765%

(g) **Weighted Average Return on Assets (WARA)**

Intangible assets, in contrast, carry a higher rate of return due to the same factors above. Averaging these rates of returns, as a percentage of the total asset base, produces a WARA. In theory, the WARA should generate the same cost of capital as the weighted average cost of capital, or WACC. The weighted average return is the sum total of the product (or multiplication) of weights that are associated with different investment options and their respective returns. The sum of such weights equals 100%

Section 50.33. In developing a discount rate, a valuer should consider:

(a) The type of asset being valued. For example, discount rates used in valuing debt could be different to those used when valuing real property or a business,

(b) The rates implicit in comparable transactions in the market,

(c) The geographic location of the asset and/or the location of the markets in which it would trade,

(d) The life/term and/or maturity of the asset and the consistency of inputs. For example, the maturity of the risk-free rate applied will depend on the circumstances, but a common approach is to match the maturity of the risk-free instrument to the time horizon of the cash flows being considered.

(e) The bases of value being applied.

(f) The currency denomination of the projected cash flows.

Section 50.34. In developing a discount rate, the valuer must:

(a) Document the method used for developing the discount rate and support its use,

(b) Provide evidence for the derivation of the discount rate, including the identification of the significant inputs and support for their derivation or source.

Section 50.35. Valuers must consider the purpose for which the forecast was prepared and whether the forecast assumptions are consistent with the basis of value being applied. If the

forecast assumptions are not consistent with the basis of value, it could be necessary to adjust the forecast or discount rate (see para 50.38).

Section 50.36. Valuers must consider the risk of achieving the forecast cash flow of the asset when developing the discount rate. Specifically, the valuer must evaluate whether the risk underlying the forecast cash flow assumptions are captured in the discount rate.

Section 50.37. While there are many ways to assess the risk of achieving the forecast cash flow, a non-exhaustive list of common procedures includes:

(a) Identify the key components of the forecast cash flow and compare the forecast cash flow key components to:

- Historical operating and financial performance of the asset,
- Historical and expected performance of comparable assets,
- Historical and expected performance for the industry, and
- Expected near-term and long-term growth rates of the country or region in which the asset primarily operates,

(b) Confirm whether the forecast cash flow represents expected cash flows (ie, probability-weighted scenarios), as opposed to most likely cash flows (ie, most probable scenario), of the asset, or some other type of cash flow,

(c) If utilizing expected cash flows, consider the relative dispersion of potential outcomes used to derive the expected cash flows (eg, higher dispersion may indicate a need for an adjustment to the discount rate),

(d) Compare prior forecasts of the asset to actual results to assess the accuracy and reliability of managements' estimates,

(e) Consider qualitative factors, and

(f) Consider the value indications such as those resulting from the market approach.

Section 50.38. If the valuer determines that certain risks included in the forecast cash flow for the asset have not been captured in the discount rate, the valuer must

1) Adjust the forecast, or

2) Adjust the discount rate to account for those risks not already captured.

(a) When adjusting the cash flow forecast, the valuer should provide the rationale for why the adjustments were necessary, undertake quantitative procedures to support the adjustments, and document the nature and amount of the adjustments,

b) When adjusting the discount rate, the valuer should document why it was not appropriate or possible to adjust the cash flow forecast, provide the rationale for why such risks are not otherwise captured in the discount rate, undertake quantitative and qualitative procedures to support the adjustments, and document the nature and amount of the adjustment.
The use of quantitative procedures does not necessarily entail quantitative derivation of the adjustment to the discount rate. A valuer need not conduct an exhaustive quantitative process but should take into account all the information that is reasonably available.

Section 50.39. In developing a discount rate, it may be appropriate to consider the impact the asset's unit of account has on unsystematic risks and the derivation of the overall discount rate.
For example, the valuer should consider whether market participants would assess the discount rate for the asset on a standalone basis, or whether market participants would assess the asset in the context of a broader portfolio and therefore consider the potential diversification of unsystematic risks.

Section 50.40. A valuer should consider the impact of intercompany arrangements and transfer pricing on the discount rate.
For example, it is not uncommon for intercompany arrangements to specify fixed or guaranteed returns for some businesses or entities within a larger enterprise, which would lower the risk of the entity forecasted cash flows and reduce the appropriate discount rate.
However, other businesses or entities within the enterprise are deemed to be residual earners in which both excess return and risk are allocated, thereby increasing the risk of the entity forecasted cash flows and the appropriate discount rate.

VALUATION TABLES	
Note: C= Capital N = Number of years R= Rate of interest T = income tax rate	
1. Simple Interest	P x N x R
2. Compound Interest (Amount of Re 1)	P x $(1 + R)^n$
3. Capitalized Value (CV)	Net Income x Years' Purchase
4. Years' Purchase	100 / Rate of Return

5. Present Value / discount rate (PV)	C X $\frac{1}{(1+R)^n}$
6. Amount of Re1 per Annum	C X $\frac{((1+R)^n-1)}{R}$
7. Gross Sinking Fund	C x $\frac{R}{(1+R)^n-1}$
8. Present value of future income Single rate (C x YP)	C x $\frac{1-\frac{1}{(1+R)^n}}{R}$ = C x $\frac{1-PV}{R}$
9. Present value of future income (Dual rate)	$\frac{1}{R+S}$ = $\frac{1}{\text{Capitalisation Rate+Sinking Fund}}$
10. Present value, adjusted for tax **'t'**	PV = $\frac{1}{(1+\text{R}\left(100-\frac{\text{t}}{100}\right)}$
11. Years' Purchase of reversion to a property	$\frac{1}{\text{r}(1+r)^n}$
12. Basic Finance Weighted Capitalization	Actual Rate = Mortgaged fund (borrowed) + Equity Fund (own)

Comments on Leasehold Properties: Before venturing in to income approach method for leasehold properties, the valuer should consider the following:

1. The genuine of the lease agreement, 2. Ascertain the contractual rent comparable to the prevailing market rent, 3. The terms and conditions of agreement and 4. Other factors associated on the lease hold properties have to be thoroughly identified.

For example, **if the plot is not fully developed but is underutilized,** in such a case, the Lessee would also hold interest equivalent to the present worth of the unutilized FSI land.

However**, if leased land is owned by a public body** like Port Authority, Municipal / Government Industrial Corporation, State Government or Central Government, the criteria of lease rent fixation are quite different.

Valuer has to consider the following points before valuing a leasehold property.

1. The total period of Lease and the unexpired period of Lease. Whether Lease is renewable for further term OR on maturity of lease period the property would revert back to Lessor.

2. What is covenant concerning status of building erected on the plot. On maturity of Lease period, the structure done by the lessee, may be demolished or retained and handed over to the Lessor. On maturity, building may vest with lessor, at free of cost or on payment of depreciated cost of building.

3. Lease rent is payable by the lessee and whether there is a provision for periodical increase in lease rent. In case of renewal of lease, what will be the lease rent for the 2nd period of lease?

4. Difference in lease rent in renewal clause, will be same as for 1st period or revised rent for the 2nd period or will it be based on prevalent market rent on date of maturity. The amount, payable to lessors (Unearned Increase) in case of Transfer / Assignment of the property during lease period.

While fixing renewal lease rent for the 2nd period

1. As in the case of renewal of lease, while fixing renewal lease rent for the 2nd period while applying investment theory of lease rent fixation. The lessor is not free to lease the property to the third party but is bound to renew lease with the sitting lessee only. It is the case of closed market for rent fixation. There are no competing tenants bidding for lease rent in the market as is the case for first time leasing of the property. Closed market or lack of competing tenants means low rental. The lessor is bound to decrease the lease rent depending on the situation.

2. The land offered for lease renewal is not an open virgin land as is the case for first time lease but is encumbered with the structure erected by the lessee.

Obviously, land value under investment theory has to be discounted for this reason.

3. Even otherwise value of land to the lessor on date of renewal is less because of further renewal period. Its present worth is only deferred value of land and not value as if freehold.

Hence, yield has to be worked out on deferred value of land which is its market worth on date of renewal of lease. Hence, the valuation process MUST involve:

1. Identify the current rent and rent review pattern
2. Identify/calculate the future rentals
3. Capitalise each block of rents using a YP (to find their future CV)
4. Discount the future CV of each block to find its PV
5. Add up all the discounted PV's to find the total present capital value of the property

The valuers can deviate from the prescribed method of valuation, for a specific case, specific purpose, as long as we are able to judiciously apply our mind and adopt a suitable method and justify the same. And finally, by adopting the appropriate method required for that specific purpose, for that specific case, we can arrive at a fair value which will in turn makes one, a recognized valuer

* * *

GENERAL STANDARDS IVS 105

2. VALUATION APPROACHES AND METHODS

2.2. MARKET APPROACH

Section 20. Market Approach

Section 20.1. The market approach provides **an indication of value by comparing the asset with identical or comparable (that is similar) assets for which price information** is available.

Section 20.2. The market approach should be applied and afforded significant weight under the following circumstances:

(a) The subject asset has recently been sold in a transaction appropriate for consideration under the basis of value,

(b) The subject asset or substantially similar assets are actively publicly traded, or

(c) There are frequent and / or recent observable transactions in substantially similar assets.

Section 20.3. Although the above circumstances would indicate that the market approach should be applied and afforded significant weight, when the above criteria are not met, the following are additional circumstances where the market approach may be applied and afforded significant weight.

When using the market approach under the following circumstances, a valuer should consider whether any other approaches can be applied and weighted to corroborate the value indication from the market approach:

(a) Transactions involving the subject asset or substantially similar assets are not recent enough considering the levels of volatility and activity in the market.

(b) The asset or substantially similar assets are publicly traded, but not actively.

(c) Information on market transactions is available, but the comparable assets have significant differences to the subject asset, potentially requiring subjective adjustments.

(d) Information on recent transactions is not reliable (ie, hearsay, missing information, synergistic purchaser, not arm's-length, distressed sale, etc).

(e) The critical element affecting the value of the asset is the price it would achieve in the market rather than the cost of reproduction or its income-producing ability.

Section 20.4. The heterogeneous nature of many assets means that it is often not possible to find market evidence of transactions involving identical or similar assets. Even in circumstances where the market approach is not used, the use of market-based inputs should be maximized in the application of other approaches (eg, market-based valuation metrics such as effective yields and rates of return).

Section 20.5. When comparable market information does not relate to the exact or substantially the same asset, the valuer must perform a comparative analysis of qualitative and quantitative similarities and differences between the comparable assets and the subject asset.
It will often be necessary to make adjustments based on this comparative analysis. Those adjustments must be reasonable and valuers must document the reasons for the adjustments and how they were quantified.

Section 20.6. The market approach often uses market multiples derived from a set of comparable, each with different multiples. The selection of the appropriate multiple within the range requires judgment, considering qualitative and quantitative factors.

Section 30. Market Approach Methods

Comparable Transactions Method

Section 30.1. The comparable transactions method, also known as the guideline transactions method, utilizes information on transactions involving assets that are the same or similar to the subject asset to arrive at an indication of value.

Section 30.2. When the comparable transactions considered involve the subject asset, this method is sometimes referred to as the prior transactions' method.

Section 30.3. If few recent transactions have occurred, the valuer may consider the prices of identical or similar assets that are listed or offered for sale, provided the relevance of this information is clearly established, critically analyzed and documented.
This is sometimes referred to as the comparable listings method and should not be used as the sole indication of value but can be appropriate for consideration together with other methods.

When considering listings or offers to buy or sell, the weight afforded to the listings/ offer price should consider the level of commitment inherent in the price and how long the listing/offer has been on the market**.**

For example, an offer that represents a binding commitment to purchase or sell an asset at a given price may be given more weight than a quoted price without such a binding commitment.

Section 30.4. The comparable transaction method can use a variety of different comparable evidence, also known as units of comparison, which form the basis of the comparison. For example, a few of the many common units of comparison used for real property interests include price per square foot (or per square metre), rent per square foot (or per square metre) and capitalization rates.

The units of comparison used by participants can differ between asset classes and across industries and geographies.

Section 30.5. A subset of the comparable transactions' method is matrix pricing, which is principally used to value some types of financial instruments, such as debt securities, without relying exclusively on quoted prices for the specific securities, but rather relying on the securities' relationship to other benchmark quoted securities and their attributes (ie, yield).

Section 30.6. The key steps in the comparable transactions' method are:

(a) identify the units of comparison that are used by participants in the relevant market,

(b) identify the relevant comparable transactions and calculate the key valuation metrics for those transactions,

(c) perform a consistent comparative analysis of qualitative and quantitative similarities and differences between the comparable assets and the subject asset,

(d) make necessary adjustments, if any, to the valuation metrics to reflect differences between the subject asset and the comparable assets (see para 30.12(d)),

(e) apply the adjusted valuation metrics to the subject asset, and

(f) if multiple valuation metrics were used, reconcile the indications of value.

Section 30.7. A valuer should choose comparable transactions within the following context:

(a) Evidence of several transactions is generally preferable to a single transaction or event,

(b) Evidence from transactions of very similar assets (ideally identical) provides a better indication of value than assets where the transaction prices require significant adjustments,
(c) Transactions that happen closer to the valuation date are more representative of the market at that date than older / dated transactions, particularly in volatile markets,
(d) For most bases of value, the transactions should be “arm’s length” between unrelated parties,
(e) Sufficient information on the transaction should be available to allow the valuer to develop a reasonable understanding of the comparable asset and assess the valuation metrics/comparable evidence,
(f) Information on the comparable transactions should be from a reliable and trusted source,
(g) Actual transactions provide better valuation evidence than intended transactions.

Section 30.8. A valuer should analyze and make adjustments for any material differences between the comparable transactions and the subject asset. Examples of common differences that could warrant adjustments may include, but are not limited to:
(a) Material characteristics (age, size, specifications, etc),
(b) Relevant restrictions on either the subject asset or the comparable assets,
(c) Geographical location (location of the asset and/or location of where the asset is likely to be transacted/used) and the related economic and regulatory environments,
(d) Profitability or profit-making capability of the assets,
(e) Historical and expected growth,
(f) Yields/coupon rates,
(g) Types of collateral,
(h) Unusual terms in the comparable transactions,
(i) Differences related to marketability and control characteristics of the comparable and the subject asset,
(j) Ownership characteristics (eg, legal form of ownership, amount percentage held).

Guideline publicly-traded comparable method
Section 30.9. The guideline publicly-traded method utilizes information on publicly-traded comparable that are the same or similar to the subject asset to arrive at an indication of value.
Section 30.10. This method is similar to the comparable transactions’ method. However, there are several differences due to the comparable being publicly traded, as follows:

(a) The valuation metrics/comparable evidence are available as of the valuation date,
(b) Detailed information on the comparable are readily available in public filings, and
(c) The information contained in public filings is prepared under well understood accounting standards.

Section 30.11. The method should be used only when the subject asset is sufficiently similar to the publicly-traded comparable to allow for meaningful comparison.

Section 30.12. Key steps in guideline publicly-traded comparable method is to:
(a) Identify the valuation metrics/comparable evidence that are used by participants in the relevant market,
(b) Identify the relevant guideline publicly-traded comparable and calculate the key valuation metrics for those transactions,
(c) Perform a consistent comparative analysis of qualitative and quantitative similarities and differences between the publicly-traded comparable and the subject asset,
(d) Make necessary adjustments, if any, to the valuation metrics to reflect differences between the subject asset and the publicly-traded comparable,
(e) Apply the adjusted valuation metrics to the subject asset, and
(f) If multiple valuation metrics were used, weight the indications of value.

Section 30.14. A valuer should analyze and make adjustments for any material differences between the guideline publicly-traded comparable and the subject asset. Examples of common differences that could warrant adjustments may include, but are not limited to:
(a) Material characteristics (age, size, specifications, etc),
(b) Relevant discounts and premiums (see para 30.17),
(c) Relevant restrictions on either the subject asset or the comparable assets,
(d) Geographical location and the related economic and regulatory environments,
(e) Profitability or profit-making capability of the assets,
(f) Historical and expected growth,
(g) Differences related to marketability and control characteristics of the comparable and the subject asset,
(h) Type of ownership.

Other Market Approach Considerations

Section 30.15. The following paragraphs address a non-exhaustive list of certain special considerations that may form part of a market approach valuation.

Section 30.16. Anecdotal or "rule-of-thumb" valuation benchmarks are sometimes considered to be a market approach. However, value indications derived from the use of such rules should not be given substantial weight unless it can be shown that buyers and sellers place significant reliance on them.

Section 30.17. In the market approach, the fundamental basis for making adjustments is to adjust for differences between the subject asset and the guideline transactions or publicly-traded securities. Some of the most common adjustments made in the market approach are known as discounts and premiums.

(a) **Discounts for Lack of Marketability (DLOM)** should be applied when the comparable are deemed to have superior marketability to the subject asset.

A DLOM reflects the concept that when comparing otherwise identical assets, a readily marketable asset would have a higher value than an asset with a long marketing period or restrictions on the ability to sell the asset.

For example, publicly-traded securities can be bought and sold nearly instantaneously while shares in a private company may require a significant amount of time to identify potential buyers and complete a transaction.

Many bases of value allow the consideration of restrictions on marketability that are inherent in the subject asset but prohibit consideration of marketability restrictions that are specific to a particular owner.

DLOMs may be quantified using any reasonable method, but are typically calculated using option pricing models, studies that compare the value of publicly-traded shares and restricted shares in the same company, or studies that compare the value of shares in a company before and after an initial public offering.

(b) **Control Premiums** (sometimes referred to as Market Participant Acquisition Premiums or MPAPs) and Discounts for Lack of Control (DLOC) are applied to reflect differences between the comparable and the subject asset with regard to the ability to make decisions and the changes that can be made as a result of exercising control.

However, participants' willingness to pay a Control Premium or DLOC will generally be a factor of whether the ability to exercise control enhances the economic benefits available to the owner of the subject asset.

Control Premiums and DLOCs may be quantified using any reasonable method, but are typically calculated based on either an analysis of the specific cash flow enhancements or reductions in risk associated with control or by comparing observed prices paid for controlling interests in publicly-traded securities to the publicly-traded price before such a transaction is announced.

The guideline transactions in the guideline transaction method often reflect transactions of controlling interests. When using that method to value a subject asset that reflects a minority interest, a DLOC may be appropriate.

(c) **Blockage discounts** are sometimes applied when the subject asset represents a large block of shares in a publicly-traded security such that an owner would not be able to quickly sell the block in the public market without negatively influencing the publicly-traded price. Blockage discounts may be quantified using any reasonable method but typically a model is used that considers the length of time over which a participant could sell the subject shares without negatively impacting the publicly-traded price

(Example: Stigma factors, **Racial habitation, Religious and personal factors)**

Notes:

1. Valuation Approaches are based on the economic principles of Principles of Price equilibrium, Principles of Anticipation of benefits and Principles of Substitution

Demand and supply factor and quality of product are equally important in determining exchange value in real markets, commodity market and stock markets. The concept 'Market is Supreme and Highest and best use' is applicable as all the appurtenant factors are considered while finalizing the price factor of the asset. Market approach is basically operating on the principle of substitution.

a) Firstly, utility of the property involving existing and future benefits due to possession and use of the property is the factor affecting the market value.

b) Secondly, there must be a demand for the property.

c) And thirdly, the property must be transferable with a clear proper title.

There are two types of properties related to market approach.

Marketable properties are broadly classified – residential apartments, houses, shops, office and industrial Non- marketable properties – educational institutions, temples, museum, public and government buildings, etc.
Under the market approach method, valuation can be done for marketable properties. For non-marketable properties either by cost approach or income approach method (if it is an income generation property) has to be followed.

2. The Comparison Method is the simplest and most direct case of using comparable evidence for the purpose of valuation. If data of similar property transactions are directly available in the market then such data can be directly used as comparable evidence. The method is however applied extensively in the residential and commercial sectors.

3. The Investment or Income Capitalization Method is used where rental data of properties are available in the market. Since capital value of a property is derived from the net rent and yield for capitalization, these two data are investigated in the market for applying in the valuation method. Obviously, comparable evidence of rental values and yields are required to be made available for the purpose of valuation. So, although the method is designated as the investment method, the basic ingredients and steps are dependent on comparison or comparable evidence.

4. Sales comparison method (direct market comparison method)
Sales comparison method is based on principle of comparison and substitution of value. Difference of value attributes with respect to price and quality of similar properties has to be investigated and suitable discounting factor with supporting evidence must be applied for the specific property.

5. Comparable Sales
Data collection sources: Sales recorded in Registration Departments, Local broker / real estate agents, Newspaper advertisement, Land acquisition cases, Auction sales information, Data bank by valuers' fraternity

Details that has to be collected: Area of plot as conveyed, Area of plot as per revenue records, Area of plot as shown in approved plan, Area of plot as per actual survey by the valuer, Correlation of four boundaries with respect to all above

Analysis of data of collected sale instances: Marketability of property, Location of the subject property, Size of the property – frontage, shape, local body regulations on land use, FSI, other contrary attributes, Property may be a tenanted or leased out, Mortgaged property, Property's controlled rental income under rent control act

Comparable sale analysis: Amount paid by parallel economy aspect, Sale may be a distress sale as per comparable sale instance, Sale may be a premium or a speculative value as per comparable sale instance, Comparable sale may be for a larger plot, Comparable sale property may be too far away from this subject property, Comparable sale done not at arm's length (sold by gift, to relatives), Comparable sale taken place much earlier – time factor

6. Factors affecting property value:

In order to adopt different market conditions, the buyers and sellers consider various characteristics of the properties. Its usage, physical benefit, service life, resale value, infrastructure facilities, civic amenities, etc. Various market forces and characteristics influence the price factor of the properties viz. Economic factor, Physical factor, Social factor & Legal factor

6.1. Economic factor

Economic factor can be of micro level (local aspects) or macro level (national aspects).

Microeconomic factor includes local population, employment opportunities, changes in services, trade and commerce, per capita income at city / district / state level, trend in city growth or expansions etc.

Macroeconomic factor includes domestic savings, fixed capital formation in real estate sector, capital investment flow in bank deposits, shares, debentures, government securities.

Factors affecting value by economic factor:

1. Demand and supply of properties,
2. Government polices (Central / State) for land development,
3. Government economic and taxation policies,
4. Resident's income, wage level, saving trend and paying capacity,
5. Money market situation,
6. Cyclical boom and recession period in real estate market,
7. Expected rental yields and return from investments,

8. Availability of money on credit from financial institutions,
9. Interest rate offered for credit from financial institutions,
10. Property tax burden and maintenance outgoes,
11. Better alternative use against current inferior use,
12. Employment potential and development potential,
13. Availability of alternate asset in the market,
14. Local population and per capita income

6.2. Physical factor (Technical Factor)

1. Land character – size, shape, area, outlook, frontage, orientation, soil type, topography
2. Infrastructure – roads, good roads networks, water supply, sanitary, drainage system, electrical power supply, telecommunication networks
3. Prominence and placement – main road, bye lane, remote area location
4. Building character- RCC Framed / load bearing structure, specification (civil, electrical, water supply, sanitary), building age and expected future life, deterioration, building cracks and present conditions, aesthetics and workman quality, obsolescence due to change in life style or technology concept, maintenance and repair liability
5. Functional aspect – optimum space use, good planning and design, high utility value, modern habitual style
6. Amenities – swimming pool, garden, lift, security system, car parking, health club, play area and compound wall
7. Environmental aspect – Noise, air, water pollution level, sea or water body frontage, vibration and noise due to nearby railway track, airport or industries and climatic conditions
8. Natural calamity – Earthquake prone, flooding due to low lying, cyclones, Tsunami prone

6.3. Social factor

1. Locality – life style and living standards in the locality (Poor class, middle class, posh areas)
2. Neighbourhood – well developed, less developed, under developed, slums, cremation ground, cemetery, garbage dumping yard, nuisance due to nearby community hall, cinema theatres, schools and colleges
3. Civic amenities – proximity to shops, malls, market, schools and colleges, community hall, hospital, railway station, bus stand, garden
4. Population – density in area, population growth, congestion

5. Means of communication – railways, roads, airports and seaport
6. Prestige aspect – prestigious building, prominent location, renowned personality as neighbor
7. Political factor – Linguistics, religious communal unrest
8. Racial habitation – Hindu colony, minority colony, Christian colony, backward community colony
9. Religious factor – nearby temples, church, mosque, place of worship
10. Personal factors – sentimental value, vasthu belief, speculative interest, specific liking for that area
11. Stigma factor – haunted house, three road junction plots, fear over the past cyclone / tsunami effect, murder or suicide in the property, land used previously as cemetery.

6.4. Legal factor

1. Social legislation – Rent control act
2. Land reforms legislation – urban land ceiling act
3. Ecological legislation – coastal regulation act
4. Transfer of property act with lease provisions
5. Land acquisition act
6. Laws governing land – Town planning act, Municipal Corporation Act, urban land ceiling act, Rent control act
7. Laws governing building construction – DCTP, LPA, development control rules, building byelaws, town planning and zoning regulations
8. Law on earthquake resistant buildings
9. Wealth tax, Income tax, capital gains tax, etc. and reservations under different acts

7. Legal Factors affecting land value

National Highway Act and Railways Act regulates development in the plot prescribing restrictions of No Construction Zone for a certain distance inside the plot from Highway centre / boundaries. Acquisition of land for road widening or for public purpose leads to reduction in value. For a smaller plot this restriction result in an unbuildable area in the plot and the value of the plot naturally reduces drastically.

Civil Aviation Authority regulates and restrict height of the building in the vicinity of air ports. This results in low consumption of FSI on the plot and ultimately to a market value reduction.

Building bylaws: Every local authority and municipal corporation prescribe rules, byelaws and regulations for development and constructions within its jurisdiction.

The building byelaws or development control rules affect the market value. Important provisions are floor space index, open space rules and height restrictions.

Market of the land will be less for those using as residential purpose and higher for commercial purpose.

Coastal Regulation Zone regulates and restrict development on all lands falling 500 metres distance from high tide level.

Waterbodies Regulation: Sometimes necessary clearance to be sought for properties near irrigation channels, water bodies, rivers. This amount to reduction of market value.

Hill Conservation Regulations: In hilly areas, restriction towards minimum land area of 20 cents in some areas, height restrictions, FSI regulations and land use etc.

In some cases, the permisible FSI cannot be achieved. This provision reduces the market value..

For larger plots open space reservation is a must. The usable area for development is restricted towards OSR. The current use of the land at future date may be changed due to town planning rules.

Contemplation of conversion of land use at a future date will have a say on the market value.

Indian Electricity Act regulates the development of land under power transmission lines. No plot can be developed under if an HT power line transmission passing. A safety distance has to be maintained on either side of the HT power line transmission. The portion of land affected depreciates in market value.

8. Market value determination

Prevailing market rate of properties is an outcome of demand, supply, merits, demerits and various locational, social, economic, political factors and circumstances.

We are valuing the assets through elucidation by prevailing market rate through market survey like dependable data, sale instances, local real estate developers/ brokers, verbal enquiries in surrounding areas. As of now, Real estate value experiencing buoyancy due to various government regulatory implications and stable markets.

The demonetization of high denomination currency notes by the Government of India has brought in impairment loss in market value of cash in individual's hand, prompted correction in real estate valuations. Moreover, the reduction in Guideline rates, the Regularization Rule for the properties by the various State Governments has also sparked the real estate

valuations along with other Central Government Acts like Benami Transactions (Prohibition) Act, Goods and Services Act, Companies Act and Real Estate (Regulation & Development) Act. With the introduction of The Insolvency and Bankruptcy Code, 2016 the ease of doing business in India has taken a fresh turn. Under SARFAESI Act 2002, while it would take an average of four years for recovery of dues under previous regulations, The Insolvency and Bankruptcy Code, 2016 lays down a remarkable recovery time of eleven months and the recovery rate is expected to be considerably more as compared to twenty per cent in the earlier regime.

So, now it is not possible to estimate the market trend in the absence of dependable data on the above said sources. Any valuation carried out requires a revalidation period and subject to review after stabilization of Indian economy and real estate market. To cope up, the valuers have to develop a capacity to create and use the technology and must be well versed in latest Acts and Amendments. Technology and upgradation of knowledge alone can provide the means of modifying the environment.

9. Lapses in Guideline Rate

1. Guideline rate remains the same irrespective of supply and demand whereas the market value changes according to the demand.
2. Guideline rate is the same for marketable and non-marketable properties, whereas no market value can be certified for non-marketable properties.
3. Guideline rate is the same even for encumbered properties whereas market value will be definitely less for encumbered properties.
4. Guideline rate is the same for land locked lands, recess plots, tandem plots, narrow pathway, etc. whereas the market value will be varying for such properties.
5. Guideline rate may be uniform for all the properties located on a single road or for a single survey number whereas the market value may differ even for adjacent properties due to any number of reasons.
6. The guideline rate may be constant for many years due to government policy decision, but the market value variation will be changing frequently.

10. Guideline rate adoption

The prevailing Market Rate / Price trend of the Property from property search sites, or the prevailing Guideline Rate of the subject property forms the basic structure for valuation through documentary evidence.

In the valuation process market rate proposed by the valuer over and above the known data collected through comparable sales or the Guideline value provided in the State Govt. notification or Income Tax Gazette, the valuer has to justify the adopted rate as the true market rate.

Any variation of 20% or more on the known market rate, validation on variation has to be given. Again, confirmation and substantiation of the Fair market Value of the asset with proper evidence has to be demonstrated according to standards**.**

We must remember that, two properties are not identical or similar. The fair market value need not be the same for these properties, the fair market value depends on various property attributes for each asset.

This will have a consideration of time angle, situation angle and other specifications involved. For this purpose, necessary weightages for the asset characters has to be determined on the basic evidence of the value.

Again, these attributes are based on the economic, physical, social and legal factors or location, size, time aspect, age and physical state of the property.

The total number of factors affecting different aspects of real estate and causing dissimilarities between them may be much more than these factors given below.

The attributes pertinent to the subject asset, in relation to the market value, will be changing from locality to locality, time to time, depending upon the local market forces.

Therefore, a detailed market study and surveys and appropriate local enquiry on these attributes before deciding on the market value has to be done.

In most cases however, valuers generally consider four principal aspects of real estate and make an ad-hoc comparison between them to arrive at a valuation conclusion.

11. Sales comparison

Sales Comparison or Direct Market Comparison is based on Principle of Comparison and Value Substitution. Difference of value attributes with respect to price and quality of similar properties has to be investigated. Suitable discounting factor must be applied for specific property.

Where there are several Sales Comparable on showing different rates, it has been said that averaging is not permissible, if land acquired are of different types and different locations.

But where there are several sales of similar land, more or less, at the same time, prices whereof have marginal variation, averaging thereof is permissible.

It is further held that for the purpose of fixation of fair and reasonable market value of any type of land, abnormally high value or abnormally low value sales should be carefully discarded.

If number of sale deeds of the same locality and of same period with short intervals are available, average price of available number of sale deeds shall be considered as a fair and reasonable market price.

The land value can differ depending upon the extent and nature of the land sold.

A fully developed small plot in an important locality may fetch a higher value than a larger area in an undeveloped condition and situated in a remote locality.

By comparing the price shown in the transactions all variables have to be taken into consideration. The transaction in regard to smaller property cannot, therefore, be taken as a real basis for fixing the market value for larger tracts of property.

In fixing the market value of a large property on the basis of a sale transaction for smaller property, generally a deduction is given taking into consideration the expenses required for development of the larger tract to make smaller plots within that area in order to compare with the small plots dealt with under the sale transaction.

12. Steps to be followed

Collection of suitable comparable as far as possible within the same locality and as similar to the subject property and recent sale transactions as possible will be the first step.

The attributes of the comparable are then compared with those of the subject property.

We can find out all relevant factors and give positive or negative weightages over the rate of the comparable. Finally, the comparison is carried out by weighing positive weightages and negative weightages. Derivations of the market value of the subject property will be with positive and negative factor over the rate of the comparable unit.

13. Valuer approach

Documentary evidence may or may not be for the similar or identical properties in the nearby locality, and for the property under valuation, sold at a different period. Suitable additions or deletions can be made over the prevailing documentary evidentiary market rate with the credit score rating which will reflect the real market value and we can defend diligently our value with more accuracy. As per the Standards, the valuer has to follow a systematic approach with due diligence in a scientific way in adopting the fair market value.

(a) Identify comparison units used in relevant market

(b) Identify comparable transactions and calculate the key valuation matrix for the transactions

(c) Comparative analysis of qualitative and quantitative similarities and differences between comparable assets and subject asset

(d) Make adjustments, in valuation for differences between subject asset and comparable assets

(e) Apply the adjusted valuation matrix to the subject asset, and

(f) If multiple valuation metrics were used, reconcile the indications of value.

The proper weightages of each attribute should be ascertained from analysis of sale transactions in the real estate market.

There is no hard and fast rule in applying percentage as ad-hoc. But with an experienced valuer these percentage may bring good result.

A few attributes which can affect the market value is given under in the annexure as reference. And many more attributes we may find, may be there for the property while inspection. We have to consolidate all the attributes by assuming credit score for them.

The credit ratings can be applied over the prevailing market rate, obtained by documentary evidence (Guideline value / Circle Rate / Others).

Remarks: All the positive weightage on social, economic and physical factors are added to the evidentiary market rate to get a true picture of the market rate for that subject asset.

The negative weightage on social, economic and physical factors can be deducted from the evidentiary market rate.

All the positive and negative legal factors must be clearly recorded towards and for the marketability of the subject asset in the report.

The valuation report format and its supporting communication make it very clear that there must be a comment on any risk rating on the asset valuation.

Comments have to be made, on the pattern of a credit rating level that has been applied.

14. Risks Indication

It is possible that an aspect could reflect in two or more grading. For example, close proximity to a congested main road with heavy traffic, could adversely affect the appearance of the neighbourhood, detract from the outlook from the land and cause noise nuisance to the property. It could therefore affect the property risk ratings with both positive and negative factors. There may be signs that the market is starting to become significantly oversupplied or less demand as a result of a political, government regulations and legal factors exploiting

the mortgage stress. This could impact on risk ratings for reduced value next years to come, in local economy impact and market segment conditions.

Risk Rating Score: However, at the same time, good valuation reporting would see comment provided on the reason for any risk rating score, even if only one or two of them. Similarly, if a significant or important issue is explained in the report, it needs to have an appropriately high-risk rating to draw attention to it.

The following could be used as a guide:

Risk Rating '1' – No readily identifiable issue

Risk Rating '2' – Minor issue only not warranting comment

Risk Rating '3' – There is an issue for the client to note (valuer notes is for the client)

Risk Rating '4' – There is an important issue in the report for the client to consider

Risk Rating '5' – There is an extremely important / urgent issue in the report that could have a major impact on value and / or marketability.

These Risk Ratings must form a clear indication and highlighted in the end of the valuation report. Based on these Risk Ratings a discount factor can be applied for the market value derived.

15. Credit Rating:

The credit scores are an integral part of the report and without applying an appropriate score the report would clearly be failing to fulfil one of the report requirements. Credit scores and comments are mutual and intrinsic parts of the report and one must reflect the other. The Credit scores may be observed in the following grades or the valuer can choose his own credit score. The credit score given below is not a thumb rule and can be adopted and adjustments made as per site conditions.

1. Very Poor - Credit Score Nil
2. Poor - Credit Score (+ or -) 1
3. Medium - Credit Score (+ or -) 2
4. Good - Credit Score (+ or -) 3
5. Very Good - Credit Score (+ or -) 4

Valuation Process: If the credit score is 4, then all the aspects of the property on marketability, utility, demand / scarcity and transferability is very good. Again, if the score is below the medium credit score of 2, there is a question on the aspects of the property on marketability, utility, demand / scarcity and transferability, which will drastically reduce the

market value. The valuer's comment / Remarks is very much necessary to confirm his basis of adoption is correct on the particular attribute aspect.

The valuers must clearly understand and distinguish these attributes and corresponding credit score can be added towards the positive and negative factors attributed to the subject asset under valuation to the evidentiary market rate. The valuers can choose different type of credit ratings score and there is no hard and fast rule.

If these factors are considered and reported in the valuation report, the valuer has fulfilled his obligation in due diligence manner by establishing the difference between the documentary evidence and the actual facts on the market value of the subject asset under valuation.

Solution 1:	
Guideline rate per square foot	Rs ---------
Increase / decrease in value towards attributes of subject land	Say (+) or (-) ----%
Adopted Market rate for the subject land	Rs ---------
Solution 2:	
Comparable sale value per square foot	Rs ---------
Increase / decrease in value towards attributes of subject land	Say (+) or (-) ----%
Adopted Market rate for the subject land	Rs ---------

ATTRIBUTES CREDIT SCORE ADOPTION

Assumptions have to be made for the Increase / decrease in value towards attributes of subject land:

No	Attribute of subject land	Remarks	Credit Score
A	**GENERAL**		
1	**Income fetching marketable property**		
	Hotel		
	Cinema		
	Mall		
	Petrol pump		

	Industrial		
	Leasehold		
2	**Non-income fetching but marketable**		
	Self-occupied house		
	Residential Apartments		
	Shops		
	Factories		
	Freehold		
3	**Non–income fetching / non-marketable**		
	Educational Institution		
	Temple		
	Public and Govt buildings		
	Museum etc		
4	**Market Type - Based on occupancy**		
	Residential		
	Commercial		
	Industrial		
	Agricultural		
	Special purpose		
5	**Sub market Type of Residential**		
	House site		
	Individual houses		
	Apartments		
6	**Location**		

	Urban area		
	Sub urban area		
	Rural		
	High Priced		
	Medium Priced		
	Low Priced		
7	**Ownership**		
	Single		
	Joint ownership		
	Co-ownership		
	Title Defect/ pending litigation/ court stay		
	Easement rights provided or given		
	Property subject to Land acquisition act		
	Property subject to coastal regulation act		
8	**Tenancy**		
	Property tenanted		
	Rental agreement		
	Tenancy quality		
	Controlled rent (Standard rent fixed by court)		
	Contractual rent		
	Lease Agreements		
	License agreement		
	Lease Covenants		
	Lease / License Period		

	Lease Specific purpose use		
9	Enforceability aspects		
10	Marketability aspects		
B	**LAND**		
1	**Land Classification**		
	Residential		
	Commercial		
	Industrial		
	Agricultural		
	Special purpose		
2	Approved / Unapproved layout		
3	Soil Safe Bearing Capacity (Poor / Good)		
4	Size (large / small / medium)		
5	Shape (irregular / square / rectangle)		
6	Area		
7	Outlook		
8	Frontage (corner, double frontage)		
9	Orientation		
10	Soil Type-rocky soil, gravelly soil, clay soil, reclaimed soil and filled up soil		
11	Topography		
12	Tandem / Recessed Plots		
13	Land locked land		
14	Wide road		

15	Road network		
16	Prominent location		
17	Main road		
18	By-lane		
19	Remote area (village / less population)		
20	Noise, air water pollution level		
21	Sea or water body frontage		
22	Vibration and noise due to nearby railway track, airport or industries		
23	Climatic conditions		
24	Earthquake prone		
25	Cyclones prone		
26	Tsunami prone		
27	Flooding due to low lying		
28	**Locality location**		
	Poor class (slums / squatter settlements)		
	Middle class		
	Upper class		
	Posh areas		
29	**Neighborhood**		
	Well-developed		
	Less developed		
	Under developed		
	Slums		

	Cremation ground, cemetery		
	Garbage dumping yard		
	Nuisance due to nearby community hall, cinema theatres, schools and colleges		
	Near to Government banned lands Mines & Quarries		
	Surrounding area development		
30	**Civic amenities- -** Proximity to		
	Shops, malls, market		
	Schools and colleges		
	Community hall, Hospital		
	Railway station, Bus stand		
	Garden, parks		
31	**Racial habitation** - Hindu / minority / Christian colony, Backward community colony		
32	**Religious factor** Nearby temples, church, mosque		
33	**Personal factors** - Sentimental value, Vastu belief, Speculative interest, Specific liking for that area		
34	**Stigma factor -** haunted house, three road junction plots, fear over the past cyclone / tsunami effect, murder or suicide in the property, land used previously as cemetery.		
35	**Means of communication** – railways, roads, airports and seaport		
36	**Prestige aspect -** prestigious building, prominent location, renowned personality as neighbor		
37	**Population -** density in area, population growth, congestion		
38	E B power line above the property		

39	Height restriction due to Air fly zone		
40	Heritage town Zone		
41	Availability of infrastructure		
42	Non availability of infrastructure		
43	Availability of Water potential (good / poor)		
44	Natural water supply (Borewell / well)		
45	Groundwater quality (good / saline / poor)		
46	Availability of Treated water supply		
47	Availability of Sanitary system - Septic tank system or Underground Sanitary Drainage system		
48	Availability of Storm water Drainage system		
49	Availability of Electricity		
50	Telecommunication network		
51	Approved / unapproved layout		
52	Encroachment on any side		
53	Encumbrances, if any		
54	**Compliance to Departures**		
	Transfer of Property Act (Eg: POA / Minor)		
	Easement Act		
	RERA Act		
	RFCTLAAR Act		
	Railways Act		
	National Highway Act		
	Civil Aviation Authority regulations		

	Indian Electricity Act regulations		
	Building bylaws		
	Coastal Regulation Zone		
	Waterbodies Regulation		
	Hill Conservation Regulations		
	Conversion of land for other use		
C	**BUILDING**		
1	RCC framed / Load bearing		
2	Technical specification		
3	Standard / poor / Rich		
4	Plinth height		
5	Ceiling height		
6	Floor		
7	Joineries		
8	Walls specification		
9	building age		
10	Expected future life		
11	Deterioration		
12	Building cracks		
13	Water supply services		
14	Sanitary Services		
15	Electrical services		
16	Aesthetics		
17	Workmanship quality		

18	Present conditions		
19	Modern, old fashioned, plain looking		
20	Building Heritage value		
21	Optimum space use		
22	Good planning and design		
23	High utility value		
24	Modern habitual style		
25	Earthquake resistant buildings		
26	Gated Community		
27	Swimming pool		
28	Garden		
29	Presence of any other landscape elements		
30	Lift		
31	Security system		
32	Vehicle parking		
33	Health club		
34	Play area		
35	Uninterrupted power supply		
36	Compound wall		
37	Obsolescence due to life style change		
38	Obsolescence due to technology concept		
39	Open space reservation		
40	Car parking restrictions		
41	Town planning and zoning regulations		

42	Environment friendly building materials use		
43	Green Building techniques		
44	Rain water harvesting		
45	Solar heating systems		
46	Lightening systems		
47	Industrial environmental pollution nearby		
48	Industrial environmental pollution nearby due to heavy traffic		
49	System of air-conditioning		
50	Provision of firefighting		
51	**Compliance to Departures**		
	Town Planning Act		
	Municipal Corporation Act		
	Urban Land Ceiling Act		
	Development control rules		
	building byelaws		
	Planning Area / Non planning Area		
	Permissible FSI		
	Classification of locality		
	Heritage controls		
	Possibility of land conversion to another zone		
D	**DEMOGRAPHICS**		
1	Local population		
2	Employment opportunities		

3	Changes in services		
4	Trend in city growth or expansions		
5	Demand and supply of properties		
6	Government polices (Central / State) for land development		
7	Government economic and taxation policies		
8	Resident's income, wage level, saving trend and paying capacity		
9	Money market situation (Inflation Factors)		
10	Cyclical boom in real estate market		
11	Recession period in real estate market		
12	Expected rental yields and return from investments		
13	Availability of money on credit from financial institutions		
14	Interest rate offered for credit from financial institutions		
15	Property tax burden and maintenance outgoes		
16	Better alternative use against current inferior use		
17	Employment potential and development potential		
18	Availability of alternate asset in the market		
19	Local population and per capita income		
20	Less Sales Transactions frequency		
21	No Sales Transactions frequency		
22	More Sales Transactions frequency		
23	Poor Sales Transactions frequency		
24	Market heterogeneity is organised / regulated		

25	Market heterogeneity is unregulated		
26	Lack of transparency for buyer / seller		
27	Open market Sale instances		
28	Closed market Sale instances		
29	Stable market Sale instances		
30	Supply is more		
31	Supply is less		
32	Demand is more		
33	Demand is less		
E	**ASSET SALE COMPARISON**		
1	Willing buyer		
2	Willing seller		
3	Unwilling buyer		
4	Unwilling seller		
5	Asset has recently been sold for consideration		
6	Asset or similar assets are publicly traded		
7	Frequent/recent sale transactions in similar assets		
8	Time Factor for comparable sale instance		
9	Future expectations		
10	Type of property comparable sale		
	Commercial		
	Residential		
	Industrial		
	Office		

	Specific purpose building		
F	**ASSET DATA COLLECTION**		
1	Sales recorded in Registration Departments		
2	Local broker / real estate agents		
3	Newspaper advertisement		
4	Land acquisition cases		
5	Auction sales information		
6	Data bank by valuers' fraternity		
7	Area of plot as conveyed, and as per revenue records		
8	Approved / unapproved area		
9	Area of plot as shown in approved plan		
10	Area of plot as per actual survey by the valuer		
11	Four boundaries Correlation with respect to all above		
12	**Buildings technical details**		
	Layout		
	Design		
	Internal planning		
	Construction type & method		
	Specifications		
	Floor area		
	Age		
	Depreciation		
	Obsolescence etc.		

13	Marketability of property		
14	Location of the subject property		
15	Size of the property		
	frontage		
	depth		
	shape		
	facing direction		
	local body regulations on land use		
	FSI		
	other contrary attributes		
16	Property may be a Mortgaged property		
17	Owner’s occupation / tenant		
18	Property may be rented or leased out		
19	Property’s rental income might have been frozen under rent control act		
20	Location of the property- This gives accessibility to roads, services, public open spaces, proximity to amenities or undesirable features etc.		
21	Neighborhood characteristics - Use zoning or other restrictions by planning authorities, presence of slums, social aspects, historic aspects 'amenities etc.		
22	Transactional characteristics - One-time payment, stage payment, time aspects etc		
Analysis of data of collected from Comparable sale			
1	Excess Amount paid on parallel economy aspect		
2	Sale - a distress sale as per comparable sale instance		

3	Sale - premium or speculative value paid as per comparable sale instance		
4	Comparable sale property - for a larger plot, too far away from this subject property		
5	Comparable sale not done at arm's length (by gift, to relatives)		
6	Comparable sale taken place much earlier– time factor		
Investment or income capitalization method			
1	License agreement		
2	Business type of license		
3	License period		
4	License fees		
5	License premium paid		
6	Net profit of the licensee		
7	Lease agreement		
8	Lease Type (occupational, building, full repair lease)		
9	Lease agreement registered?		
10	Lease covenants		
11	Lease period		
12	Unexpired lease		
13	Provision for subleasing		
14	Lease premium		
15	Lease rent		
16	Sublease rent		
17	Outgoes		

18	Net maintainable rent		
19	Comparable evidence on rent		
20	Market rent		
21	Contractual rent		
22	Capitalization rate		
Evaluation by Profit Method			
1	Gross income for the last 3 years		
2	Average gross income		
3	Outgoes		
4	Net income		
5	Capitalization rate for tangible / intangible		
6	Any other factor affecting the value		
Risk Rating Report			
a	Risk Rating '1' – No readily identifiable issue		
b	Risk Rating '2' – Minor issue only not warranting comment		
c	Risk Rating '3' – There is an issue for the client to note (valuer notes is for the client)		
d	Risk Rating '4' – There is an important issue in the report for the client to consider		
e	Risk Rating '5' – There is an extremely important / urgent issue in the report that could have a major impact on value and / or marketability.		

JUSTIFICATION OF MARKET VALUE (SAMPLE REPORT)

1.0. Preamble:

A Valuer, had valued a textile Unit at Pudukottai District, with the land extent of 15.385 Acres and industrial building of 81393 square feet with all facilities in 2018. He has valued the land

extent @ Rs 35 lakhs per acre as market value. The guideline value for various survey numbers varies from a minimum of Rs 4,22,100 per acre to a maximum of Rs 29,18,520 per acre. The financial institution has directed the valuer for supporting statement for the market value adopted by the valuer for the variation of 20% or more on the known market rate and asked for validation on variation.

Justification Report

2. Adoption of IVSC standard:

For a valuation to be credible, it is important that the judgments are made in a way that promotes transparency and minimizes the influence of any subjective factors on the process.

2.1. IVSC IVS 410 Asset Standard, Development Property,

Section 120.1. Special Considerations for Secured Lending - it is stated that, the appropriate basis of valuation for secured lending is normally market value.

2.2. General Standards IVS 105, Valuation Approaches and Methods

Section 10.5. While this standard includes discussion of certain methods within the Cost, Market and Income approaches, it does not provide a comprehensive list of all possible methods that may be appropriate.

2.3. Summation Method

Note: Since this property is a textile unit, the procedure adopted is by summation method (Both cost and market approach). Income Approach method cannot be adopted for this type of property. A valuation method that provides an indication of the value of an entire asset by the addition of the separate values of its component parts.

Section 70.8. The summation method, also referred to as the underlying asset method, is typically used for investment companies or other types of assets or entities for which value is primarily a factor of the values of their holdings.

Section 70.9. The key steps in the summation method are:

(a) value each of the component assets that are part of the subject asset using the appropriate valuation approaches and methods, and

(b) add the value of the component assets together to reach the value of the subject asset.

Section 70.10. The cost approach should capture all of the costs that would be incurred by a typical participant.

Section 70.11. The cost elements may differ depending on the type of the asset and should include the direct and indirect costs that would be required to replace/ recreate the asset as of the valuation date.

2.4. General Standards IVS 105, Valuation Approaches and Methods - Market Approach (Note: Since, the validation of land valuation is the subject of this opinion, this method is engaged).

Section 20.3. Although the above circumstances would indicate that the market approach should be applied and afforded significant weight, when the above criteria are not met, the following are additional circumstances where the market approach may be applied and afforded significant weight.

When using the market approach under the following circumstances, a valuer should consider whether any other approaches can be applied and weighted to corroborate the value indication from the market approach:

(a) Transactions involving the subject asset or substantially similar assets are not recent enough considering the levels of volatility and activity in the market.

(b) The asset or substantially similar assets are publicly traded, but not actively.

(c) Information on market transactions is available, but the comparable assets have significant differences to the subject asset, potentially requiring subjective adjustments.

Section 30.7. A valuer should choose comparable transactions within the following context:

(a) evidence of several transactions is generally preferable to a single transaction or event,

(b) evidence from transactions of very similar assets (ideally identical) provides a better indication of value than assets where the transaction prices require significant adjustments,

(c) transactions that happen closer to the valuation date are more representative of the market at that date than older / dated transactions, particularly in volatile markets,

(d) for most bases of value, the transactions should be “arm’s length” between unrelated parties,

(e) sufficient information on the transaction should be available to allow the valuer to develop a reasonable understanding of the comparable asset and assess the valuation metrics/comparable evidence,

(f) information on the comparable transactions should be from a reliable and trusted source,

(g) actual transactions provide better valuation evidence than intended transactions.

Section 30.8. A valuer should analyze and make adjustments for any material differences between the comparable transactions and the subject asset. Examples of common differences that could warrant adjustments may include, but are not limited to:

(a) material characteristics (age, size, specifications, etc),

(b) relevant restrictions on either the subject asset or the comparable assets,

(c) geographical location (location of the asset and/or location of where the asset is likely to be transacted/used) and the related economic and regulatory environments,

(h) unusual terms in the comparable transactions,

(i) differences related to marketability and control characteristics of the comparable and the subject asset, and

(j) ownership characteristics (eg, legal form of ownership, amount percentage held).

2.5. Guideline publicly-traded comparable method

Section 30.9. The guideline publicly-traded method utilizes information on publicly-traded comparable that are the same or similar to the subject asset to arrive at an indication of value.

Section 30.10. This method is similar to the comparable transactions' method. However, there are several differences due to the comparable being publicly traded, as follows: (a) the valuation metrics/comparable evidence are available as of the valuation date,

Section 30.11. The method should be used only when the subject asset is sufficiently similar to the publicly-traded comparable to allow for meaningful comparison.

3. Tamil Nadu Registration Department Guideline value

1. Guideline rate is unscientific whereas the market value is based on the valuer's judicial approach to the problem.

2. Guideline rate may be uniform for all the properties located on a single road or for a single survey number whereas the market value may differ even for adjacent properties due to any number of reasons.

3. Due to policy revision, the local state government can lower or increase the guideline rate (Government of Tamil Nadu on June 2017 has announced that it is lowering the guideline rate by 33%) whereas the market value changes due to the real estate trend and money market prevailing on the date of valuation

4. Guideline rate remains the same irrespective of supply and demand whereas the market value changes according to the demand.

5. The guideline rate may be constant for many years, whereas the market value may even change on the next day.

6. Guideline rate is the same for all the properties irrespective of the fact whether they are marketable or non-marketable whereas no market value can be certified for non-marketable properties. Guideline rate is the same even for encumbered properties whereas market value will be definitely less for encumbered properties. Guideline rate is the same for land locked lands, recess plots, tandem plots, narrow pathway, etc. whereas the market value will be less for such properties.

7. There is a common perception and assumption taken by the Government that" the highest registered rate of the previous year is the guideline rate for the next year. The registration department revises the rates after reviewing the registrations every year.

8. Seldom do people register beyond guideline rates due to obvious reasons. Even if they do, it remains a stray case.

9 Guideline rates still remain 'arbitrary, unscientific at the whims of the ruling dispensation'. At no stretch of imagination can it be even remotely linked to market value.

10. Guideline values have been fixed for all the areas in the State. Well established residential areas have only street-based guideline values. The guideline values have been fixed for each survey number. This will remain unchanged till the next revision.

11. This guideline value helps the registered officer in the detection of prima facie undervaluation of property.

4. Court Judgments

1.. In Bombay High Court - Goa Housing Board, A Statutory ... vs Shri Pandurang V. Sawant, ... on 16 April, 2008, The court observed that, although there are different methods for arriving at the market value of the acquired land, it is now well settled that comparable sales instance method of valuation is preferred to other methods of valuation, because it furnishes the evidence of the market value. The sale must be the genuine transaction, the sale deed must have been executed at the time proximate to the date of the said notification, the land covered by the sale must be in the vicinity of the acquired land and must also be similar and comparable.

The factors affecting the value of land include size, shape, road width, locality and surroundings amenities, Floor Area ratio, and connectivity. An allowance may be made (plus or minus) on account of the difference between the comparable instance of sale due to shape,

size, road width, return frontage, time gap, set back space, plot coverage and any other features which in the opinion of the valuer will affect the value.

2. (1994) 4 Supreme court cases 595 - Jawajee Naganathan V. R.D.O.

3. (1995) 1 Supreme court cases 717 Land Acquisition officer V. Jasti Rohini

4. 1995 (II) CTC 492 (G. Loganathan V. Chenniya Chettiar)

5. Naganathan V. Revenue Divisional officer, Adilabad AIR 1983 A.P. 155

6. Collector Nilgris V. Mahavir Plantations AIR 1982 - Madras 138

7. Delhi High court - AIR 1985 - Delhi - Inderprasad V. Union of India

8. High court Allahadad State of Uttar Pradesh V. Shan Singh 1995 (1) H.V.D. 191.

9. Madras High court - Sakthi V. Shree Desigachary dt. 07.04.2006 C.R.P. 3092 of 1996

9. Ramesh Chand Bansal vs. District Magistrate, Collector, Ghaziabad, ANU / SC / 0369 / 1999: 1999 (5) SCC 62,

10. Hindustan Motors vs. Appropriate Authority, the Madras High Court on 20.10.2000,

In all the above cases, the Honourable courts held that:

Basic Valuation Register prepared and maintained for the purpose of collecting stamp duty has no statutory base or force. It cannot form a foundation to determine the market value.

Fixation of market value on the basis of the basic valuation register is illegal and unsustainable. Valuation register on the basis of the notification under section 47A of the stamp act is for collection of Revenue and it cannot be the basis for determination of market value of land.

The price which a willing seller might reasonably expect to obtain from a willing purchaser is the test to determine the market value and it cannot be based on the opinion or information given by the government.

The guideline value, contained in the basic register, maintained by the Revenue department for the purpose of stamp duty has no statutory base or face. It cannot form a foundation to determine the market value mentioned thereunder in instrument brought for registration.

5. Opinion:

5.1. Actual land area

Land owned by ---- Textiles is 11.93 acres. Another Company ------- (Same Promoter's Group) has leased out 3.455 acres to this unit for a lease period commencing from 1995. Additional land in this unit, of 3.12 acres property owned by an individual which was not considered for valuation. The actual land area of this unit is 18.505 acres. But the valuation was restricted to 15.385 acres only under the directions from the company.

5.2. Land Development:

1. The Promoters Group controls the entire area and had laid Bituminous Road all round their units and they have developed the entire area with all infrastructure facilities like water supply and electrical services.

2. For this unit, there is a direct connection with road formation from the main NH45 laid with Bituminous Road. Surrounding this industrial unit Bituminous Roads have been formed. The area that was not considered in valuation also been provided with all facilities.

3. These facilities are common to the surrounding units, being held by the Promoter Group. For the land development with the infrastructures expansion, a substantial increase in the land rate have to be projected, since we are considering the guideline value only. An of 50% in the guideline rate, based on the above facts, has to be provided in valuing this subject property under valuation.

5.3. On comparable sales

1. It may be noted that the surrounding areas are under the ownership of the Promoter group and the group controls the entire area in that locality.

2. As such, there was no evidences of comparable sale in the nearby unit area. The last sale instance in the nearby unit was in 2006 and thereafter no sale instance is available in the nearby area. Hence, the valuer has to consider only the guideline value with assumptions.

3. The available sale instance as of 2006 is older dated transactions more than 10 years old for comparison, and were unusual terms in the comparable transactions and also the transactions were not in “arm’s length” between unrelated parties. It was carried out within the Promoter Group itself. **Hence comparable sale method is not considered.**

5.4. Guideline Value

1. The guideline value reported in the valuation report shows that the guideline value for various survey numbers varies from Rs 4,22,100 to Rs 29,18,520 per acre. The average guideline value works out to Rs 16,70,310 per acre.

2. Due to policy revision, the local state government can lower or increase the guideline rate (Government of Tamil Nadu on June 2017 has announced that it is lowering the guideline rate by 33%) whereas the market value changes due to the real estate trend and money market prevailing on the date of valuation.

3. Hence the guideline rate will not reflect the market value, unless and otherwise attributes favouring the subject land is added to the guideline value to arrive at the fair market value.

6.0. Market value of this subject land

Market value can be solely determined by the market forces of the factors like economic factors demand and supply, physical factors like location, shape, etc., legal factors and social

factors. It may be noted that, Market value can be determined by demand supply with the market forces, but often it will fluctuate more.

Fair Market Value may match with market value but it will have rejection on Distress sale or forced sale transaction that could have occurred

Ind AS 113, specifies that in the absence of a principal market, the most advantageous market should be considered. The most advantageous market is the market that maximizes the amount that would be received to sell a given asset or minimizes the amount that would be paid to transfer the liability, after taking into account transaction costs and transportation costs.

Fair Value measurements should reflect market participant assumptions in pricing an asset or liability. Market participants are assumed to be buyers and sellers in the principal (or most advantageous) market that are knowledgeable independent, unrelated parties willing and able to transact for the asset or liability being Fair Valued without compulsion.

6.1. Basis of Land Valuation

In the report, it has been mentioned that, the land market value is taken as Rs 35,00,000 per acre and adopted rate as Rs 30,00,000 per acre.

General Standards IVS 104, Bases of Value Section 200. Assumptions and Special Assumptions

Section 200.1. In addition to stating the basis of value, it is often necessary to make an assumption or multiple assumptions to clarify either the state of the asset in the hypothetical exchange or the circumstances under which the asset is assumed to be exchanged. Such assumptions can have a significant impact on value.

Section 200.5. All assumptions and special assumptions must be reasonable under the circumstances, be supported by evidence, and be relevant having regard to the purpose for which the valuation is required.

In the absence any comparable sale instances, to ascertain the market value, the valuer has no other option to make assumptions. The average guideline rate is taken as the basis of working for the market rate, related factors assigning to the market value of the subject property are assumed and the market value is derived.

6.1.1.Basic Considerations

1. The property market value has been considered with reconciliation of various economic, social, physical and legal factors. Prevailing market rate is estimated through market survey like dependable data, sale instances, local real estate developers/ brokers and enquiries in surrounding areas.

2. This will have a consideration of time angle, situation angle and other specifications involved. For this purpose, necessary weightages for the asset characters has to be determined on the basic evidence of the value.

3. Again, these attributes are based on the economic, physical, social and legal factors or location, size, time aspect, age and physical state of the property.

3. As per the Standards, the valuer has followed a systematic approach with due diligence in a scientific way in adopting the fair market value. Applied the adjusted valuation matrix to the subject asset, and the proper weightages of each attribute is ascertained from analysis of sale transactions in the real estate market.

6. 2. Adjustment factors considered for valuation of this subject property

6.2.1. Basic factors

1. Surrounding areas have been developed and in future this area can be developed as an Industrial Establishments hub. Hence the Market potential for the development is good.

2. Non-financial obligations (political or social criteria): Being in an area there is no Non-financial obligations till now

3. Legal permissions or zoning: Away from the National Highway and also in located in an area where there are no zoning regulations

4. Conditions or constraints on permitted development: Nil

5. Limitations, encumbrances or conditions imposed: Nil

6. Rights of access to public highways or other public areas: The unit has its own road to the main National Highway

7. Geotechnical conditions: Good

8. Potential for contamination or other environmental risks: Nil - Absence of environmental pollution in vicinity of property in terms of industry, heavy traffic

9. Already Available of improve needed for services

10. Need for any infrastructure improvements: Already Provided

The property qualifies for the above-mentioned attributes towards market value. These attributes carry an adjustment factor of 20% on the market value of the asset under valuation.

6.2.2. Property Characteristics

1. Located in Non-Planning Area as per Master Plan provisions related to property in terms of land use.

2. FSI well within the allowable limits & Ground coverage is 7.96%

3. Transferability of developmental rights can be done

4. The buildings in the property is as per the provision of Building by-laws as applicable to the property viz. setbacks, height restriction etc. The Chief Inspector of Factories had approved the Building Plan and License for the industrial unit is in force

5. Surrounding land uses & adjoining properties in terms of uses are Industrial Establishments and uncultivated dry Agricultural lands.

6. There is no agreement on easements, acquisition notifications for road widening or for others and there are no heritage restrictions.

7. The property is SARFAESI compliant

8. Electrical service connection is for 900 KW and all property taxes are paid up to date

9. The location of the property is well and directly connected to the National Highway. 10. Also, with in terms of social structure of the area, population, social stratification, regional origin, economic level, is good.

11. Hence the location and situation attributes are good in marketability of this asset.

This property meets the requirements for the above-mentioned attributes towards market value. These attributes carry an adjustment of 20% on the market value of the asset under valuation.

6.2.3. Current Use / Existing Use

As per IVSC General Standards, IVS 104 Bases of Value, in Section 150.1. Premise of Value – Current Use / Existing Use - The highest and best use for an asset may be its current or existing use when it is being used optimally. And also, in Section 160.2. The reasonable period of time to find a purchaser (or purchasers) may vary by asset type and market conditions.

Remarks: Since this unit is in running condition, it is assumed as existing use as it is being used optimally is the highest and best use for this asset. These attributes carry an adjustment factor of 5% on the market value of the asset under valuation.

Land Valuation Justification	
Land value adopted by the valuer Average Guideline rate prevailing on the date of valuation	Rs 16,70,310 /- acre
2. Additions - 1. Land development factors (Bitumen roads & services) 50 % on Rs 16,70,310 /- acre	Rs 8,35,155 /- acre
3. Basic factors (As Noted above) 20% on Rs 16,70,310 /- acre	Rs 3,34,062 /- acre
4. Property Characteristics 20% on Rs 16,70,310 /- acre	Rs 3,34,062 /- acre

5. Current Use / Existing Use 5% on Rs 16,70,310 /- acre	Rs 83,516 /- acre
6. Total	Rs 32,57,105 /- acre
7. Deduction: Assuming if in any case of eventuality or value decrease due to recession or other reasons beyond the scope of valuer	Rs 2,57,105 /- acre
8. Adopted Rate	Rs 30,00,000 /- acre

7. Conclusion:

Based on the actual facts and information and relevant document materials given to me, I am of the opinion that the Market value certified by me in my report is justifiable and reasonable under all Departures as per IVSC.

I hereby declare that:

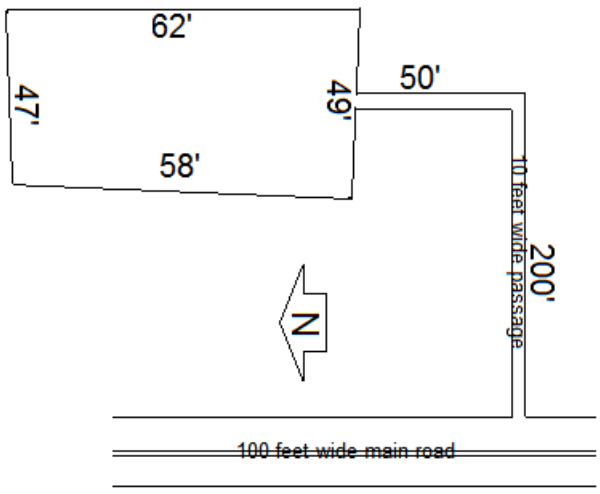
1. The information provided is true and correct to the best of my knowledge and belief.

2. The analysis and conclusions are limited by the reported assumptions and conditions.

3. I have followed the provisions of the IBA and IVSC to the best of my ability and this report is in conformity to the Standards of Reporting

4. Fair Market Value may match with market value but it will have rejection on Distress sale or forced sale transaction that could have occurred

MARKET APPROACH - CASE STUDY 1



1. The property is a **vacant land of 2880 square feet** situated in a well-developed prominent locality in a city commanding all facilities.

2. The subject property is an **irregular shaped** one. On the North 47 feet, South 49 feet, East 62 feet and West 58 feet.

3. The approach to the site is from 10 feet wide passage connecting the 100 feet wide main road. The 10 feet passage is 250 feet length and in that the last 50 feet length take a turn and ends with the subject property.

4. The said passage is encroached with hutments and only a cycle can go through the passage. For construction of a building in the said property, the construction materials have to be manually taken that too only in the night time. Even in the night material transport is cumbersome because of the encroachment by neighbours.

5. The guideline value in that particular area is Rs 12000 per square foot. Comparable sale value from sale instance **(Commercial)** on the 100 feet wide main road with 50 feet frontage taken about 2 months back reflect the value of Rs 17200 per square foot. Determine the market value of the property.

Solution 1:	
Guideline rate per square foot	Rs 12,000
Increase / decrease in value towards attributes of subject land	(-) 60%
Adopted Market rate for the subject land per sqft	**Rs 4800/-**
Solution 2:	
Comparable sale value per square foot	Rs 17,200
Increase / decrease in value towards attributes of subject land	(-) 70%
Adopted Market rate for the subject land per sqft	**Rs 5160/-**

Note: Assumptions were made for the decrease in value towards attributes of subject land: **The subject property was sold at Rs 5500/- per sqft**

MARKET APPROACH - CASE STUDY 2

1. The property is located in SIDCO Industrial Estate. It is connected to a 50 feet main Road on the north side by a 24 feet wide passage for a length of 90 feet. The main portion lies in the rear of the land. The property is surrounded by other properties and the only entry to the main road is by the 24 feet wide passage.

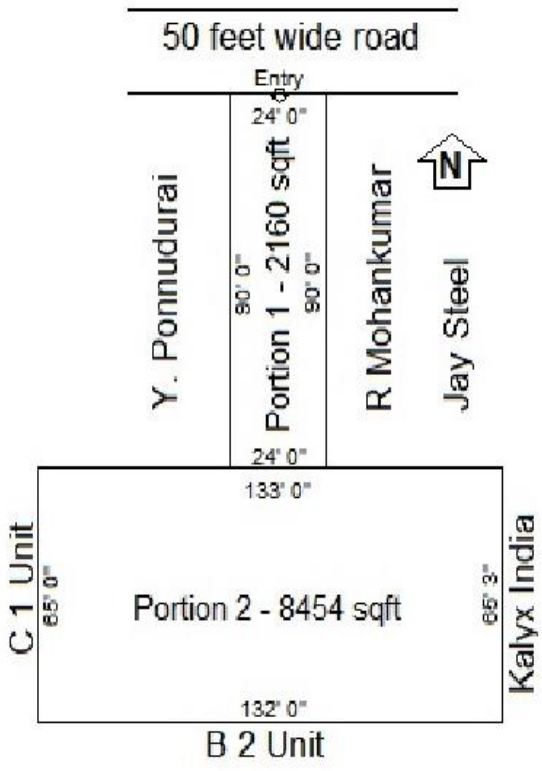
2. Extent of land area is 10614 square feet. This extent is divided in to 2 portions viz., the front portion being a passage and the rear portion is of irregular shape.

3. The **front portion** is **2160 square feet**. **It is a Narrow strip of land**. The **frontage** of the land is **only 24 feet** and **depth** of the land is **90 feet**. The depth of the plot is more when compared to frontage. This portion serves as a main entry point connecting the Main Road to the rear land.

4. The **rear portion is 8454 square feet**, with **irregular shape** having an approach to the main road through the passage area of 24 feet wide.

Comments - Front (first) portion

1. This portion as described above, is the main entry point to both the first and second portion.



It is on the main road and in line with the front adjacent properties (First Belt)

2. So as to say, the second portion has got no direct approach road connectivity. The second portion of the property is surrounded by adjacent land owners on three sides.

3. This front portion has to be treated as an **easement of necessity attached to the second portion. Hence, without this portion the rear land will become a land locked land.** So, the BUYER has to necessarily buy this easement land as a legal provision to have access to the second portion.

4. This portion is a **narrow strip of land** of 24 feet x 90 feet. The frontage is only 24 feet. The depth of the plot is more when compared to frontage. The depth of this portion is more (nearly 3.75 times) when compared to frontage.

5. In order to allow the goods transportation for the second portion, this portion has to be kept vacant. No building can be constructed in this portion.

6. The Revenue Authority has classified this property as in Industrial Zone. The Planning parameters for an industrial or an ancillary building cannot be enforced on this portion. To construct a building with side open space and set back areas and allowing vehicles in this narrow strip it will be difficult to manage.

7. The restrictions in Building Rules by Regulatory Authority, prevent for a development in the subject property. Hence, the construction development area will get reduced due to development restrictions and achieving the permissible FSI is denied due to location as well as shape and direction.

8. Owing to the first portion of 90 feet depth perpendicular to road from road side, this entire portion is un- utilizable. Marketing of development will also be challenging due to the situation.

Comments- Second (rear) portion

1. The location of the second portion is in the second belt, i.e. 90 feet away from the road. It is located behind the adjacent road facing properties.

2. In areas, where activities are predominant, the land value abutting the road will be higher as compared to the land away from the road.

Adopting the same guideline value for the main road to this portion of the property will not match with the fair market value. Hence, a discount has to be made on this account.

3. A plot of rectangular shape fetches more value than the plot of irregular shape. An adjustment factor can be applied depending upon the irregularity in shape and frontage of the plot that affect the layout of the building and general architectural planning.

4. The restrictions in Building Rules prevent for a development in the subject property. Hence, the construction development area will get reduced due to development restrictions and achieving the permissible FSI is denied due to location as well as shape and direction.

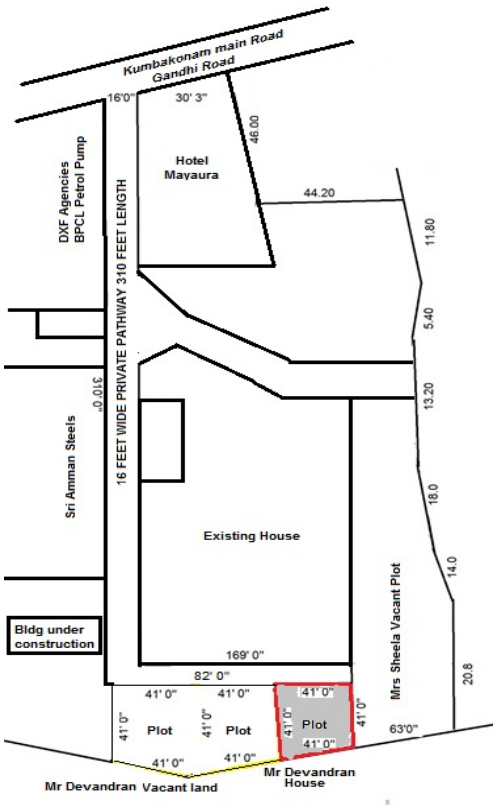
5. There is no distinct guideline value for the subject (second rear portion) property. Rs 6000 per square foot, is the value adopted for the nearby area, which is 90 feet away from the subject property. The stamp duty value as adopted by the registrar is not meant for this particular (second rear portion) property.

6. Moreover, this guideline value reflects the market value on the main road. This guideline value spreads for more than 800 metres on the main road on both sides longitudinally.

7. The market rate is Rs 6000 per square feet whereas the sale price is Rs 3300 per square feet.

MARKET APPROACH - CASE STUDY 3

1. Extent of plot is 1681 square feet
2. Property located 392 feet away in 16 feet wide private passage to main Road
3. Location- residential area
4. Located in a low-lying area
5. Lies in locality presently classified as Primary residential zone
6. Unshaped land
7. Development restrictions for building construction – only residential house project can be constructed
8. No infrastructure available
9. Approach is through mud road:
10. The property is surrounded by a private passage on the North and others property in East, West and South.



11. **Cul-de-sac**: the passage is closed at the end of the property. No further development of road is possible

12. Extreme end property and also lies in the Extreme end of the passage.

13. Stamp duty rate as on the date of sale was calculated at Rs 1452 per square foot for this property. Whereas the sale is Rs 400 per square foot.

COURT JUDGMENTS

The following judgments will be highly helpful for the practising panel valuers in order to defend when their reports are challenged in the court of law.

1. Liability against a professional arises only when he is an active participant in a plan to defraud the bank.

CBI Vs. K. Narayana Rao - Supreme Court - (2012) 9 SCC 512 - 21.09.2012.

2. Valuer is not an expert to test the genuineness of the documents.

L.N. Rajagopalan Vs State - CRL.R.C.No. 1063 of 2008 - Madras High court - 10.08.2009.

3. A valuer is not competent to certify the genuineness of the title.

Vijay Kumar Singh Vs State of Bihar - 27162 of 2011 Patna High court - 10.12.2013.

4. A valuer is not responsible to detect the forged document.

Aparna das Vs Banks - W.P.No. 22699 (W) of 2014 - Kolkata High court - 19.08.2014.

5. Valuer has no role to certify or verify the title of the documents.

Hemraj Phonsa Vs CBI - 11.12.2015 - Court of special judge, Anti-corruption, Jammu & Kashmir.

6. AIR 2000 Supreme Court 355 - from AIR 1998 - Allahabad 72. Civil appeal no. 5929 of 1997 dt. 03.12.1999.

Valuation is basically a question of fact and the court is normally reluctant to interfere with the finding on such a question of fact if it is based on relevant material on record. Valuers are technical persons. While valuing, they would have taken into consideration all aspects. Once we are convinced that the method adopted by the valuers for the purpose of valuation is based on relevant materials, then this court will not interfere with such a finding of fact.

7. Civil appeal no. 6204 of 2009 - 24.05.2012 - Supreme court.

It becomes a legal obligation on the part of the authority that property be sold in such a manner that it may fetch the best price. Thus, essential ingredients of such sale remain a correct valuation report and fixing the reserve price. It is evident that law requires a proper

valuation report. Valuation is a question of fact and valuation of the property is required to be determined fairly and reasonably.

8. Kerala High court - 1991 - 187 ITR 277 KER dt. 18.07.1990.

If anybody arrives at a value arbitrarily, such a binding is not acceptable to the court. The registered valuer has arrived at the value based on certain methodical calculation and it is acceptable to the court.

9. ITR 282 to 285 of 1980 and 431 to 438 of 1982 - 28.03.1988

Such method should be preferred which has more objective reliable data to rely upon than mere subjective opinions. Apply the well-known and recognised method and compare.

It is essential, as far as possible, to check the valuation by one method with another method provided both methods are based an objective and reliable data. In case of compensation, court's attitude is more liberal estimate and in a revenue case, it is more conservative estimate.

10. Meher & Another v Collector of Drug AIR 1979 MP 46. & Chimanlal Hargovinddas v Special L.A.O., Poona inter alia - AIR 1988 SC 1652 (1988) 3 SCC 751

Comparable sales on the basis on which the market value is to be determined should be of such lands as are (a) similar in character as can be; (b) of reasonable Proximus to the acquired land; (c) they should have similar amenities and advantages; and (d) the sale should be the true Proximus to the date of acquisition.

11. Bombay High Court - Goa Housing Board, A Statutory ... vs Shri Pandurang V. Sawant, ... on 16 April, 2008

Comparable sales instance method of valuation is preferred to other methods of valuation. Although there are different methods for arriving at the market value of the acquired land, it is now well settled that comparable sales instance method of valuation is preferred to other methods of valuation, because it furnishes the evidence of the market value of the acquired land which a willing purchaser would pay if it had been sold in the open market at the time of publication of notification under Section 4 of the Act.

The factors affecting the value of land include size, shape, road width, locality and surroundings amenities, Floor Area ratio, and connectivity. An allowance may be made (plus or minus) on account of the difference between the comparable instance of sale due to shape, size, road width, return frontage, time gap set back space plot coverage, FA and any other Features which in the opinion of the valuer will affect the value.

12. When is, the development method of valuation is the most appropriate method?

In the case of Shr iBhuvnesh Kumar Shrotiya, vs. Income Tax Officer-4(1), Agra. The IT Appellate Tribunal Agra observed on 09.07.2013

The method adopted for valuation called Development method is most appropriate and well-reasoned. The method takes permissible ground coverage and F.A.R. for marked use of land as per building bye-laws of Agra Development Authority applicable at the time of sale and prevailing market rates for land of society at the time of sale

13. Supreme Court - SLAO .vs Sidappa Omanna Tumari And Ors. Etc on 27 October, 1994

A report of an expert for establishing the market value can be acted upon by the Court if "relevant factual data or material which constituted basis for the report is also produced and the same is proved to be genuine and reliable and the method adopted by the expert is found to be recognized and correct."

14. Supreme Court - Mahesh Dattatray Thirthkar vs State of Maharashtra on 4 March, 2009, it is not necessary for the expert to rely on the report of another person with regard to the same. He, being an expert in his field, can rely on his own knowledge, experience and judgment to come to conclusions regarding the aspects of the acquired property'

15. Supreme Court - Kolkata Metropolitan vs Gobinda Chandra Makal & Anr., supreme court on 2 September, 2011

Made the following observations on the report submitted by the Expert valuer

Advantage of a better frontage is considered to be a plus factor while assessing the value of two similar properties, particularly in any commercial or residential area, when one has a better frontage than the other.

16. High Court of Madras - K.T. Venkatesan vs Appropriate Authority on 31 October, 2002,

"Merely there is a traffic meridian or traffic regulations or U-Turn traffic regulation in force to reach the property, it cannot be stated that the subject property is inferior in any way to the two comparable sales. The traffic regulation or restriction would in other words show that the subject property is located very near to the Main Road where there is heavy traffic which would mean the subject property commands more demand than the two comparable sales."

* * *

ASSET STANDARDS

3.1. IVS 400 REAL PROPERTY INTERESTS

Section 20. Introduction

Section 20.1. Property interests are normally defined by state or the law of individual jurisdictions and are often regulated by national or local legislation. Before undertaking a valuation of a real property interest, a valuer must understand the relevant legal framework that affects the interest being valued.

Notes: The highest form of estate or title to land with possession free from restrictions and encumbrances is called freehold (Fee Simple). A property owned with absolute ownership is called a real estate. This further classified as movable (land and building) and immovable (plants & machineries).

The owner is entitled to (Bundle of Rights)

a) Use of property in any manner (1) or abuse the property till it result in nuisance (2)

b) Enjoy it by exclusive possession (3)

c) Derive benefits (4), income or profits from it (5)

d) Disposing it during his lifetime by sale (6), gift (7) or will (8)

e) can grant lease (9), create mortgage (10), induct license (11)

Absolute ownership of Real Estate means that the owner holds each and every right described. He can part with some of these rights for consideration or otherwise and still continue to own the property. Owner enjoys all these rights till perpetuity as ownership right is perpetual.

Ownership rights : Right of possession, Right to use and enjoy, Right to consume, Right to lease, rent, sale, transfer or assign, gift or give away under will, Owner can transfer part or whole of this right to others for a determined period as is the case in lease and license, Right to develop, Heritable right, Residuary right:

The owner of property holds residuary powers in case of lease, license or mortgage. Residuary rights are permanently held by the owner unless the same are sold or gifted. All these rights are popularly known as bundle or rights.

Section 20.2. A real property interest is a right of ownership, control, use or occupation of land and buildings. There are three main types of interest:

(a) the superior interest in any defined area of land. The owner of this interest has an absolute right of possession and control of the land and any buildings upon it in perpetuity, subject only to any subordinate interests and any statutory or other legally enforceable constraints,

Notes: The land ownership is affected by government in three categories.

1) Government imposes taxation and the right to impose compulsory acquisition on any property.

2) Right to take or revert back any property in the absence of any legitimate inheritance.

3) Government also imposes restrictions on land use and rights of interest by development through zoning regulations, Environmental requirements

(b) a subordinate interest that normally gives the holder rights of exclusive possession and control of a defined area of land or buildings for a defined period, eg, under the terms of a lease contract, and / or

(c) a right to use land or buildings but without a right of exclusive possession or control, eg, a right to pass over land or to use it only for a specified activity.

Note.1 - A leasehold interest in the property is the right to occupy and use the property for a fixed term or perpetuity as per the terms and conditions in the lease deed. Lessee as per terms and conditions can develop, sub lease it, and enjoy benefits arising out. The lessee has a right in the property and the rights can be mortgaged restricted to his leasehold interests**.**

Note.2 - A right to enter in to the land belonging to another person. The pathway rights enjoyed in another land by way of easement rights. Interests arising out of mortgagor and mortgagee in a mortgage**.**

Section 20.3. Intangible assets fall outside the classification of real property assets. However, an intangible asset may be associated with, and have a material impact on, the value of real property assets. It is therefore essential to be clear in the scope of work precisely what the valuation assignment is to include or exclude. For example, the valuation of a hotel can be inextricably linked to the hotel brand.

In such cases, the valuation process will involve consideration of the inclusion of intangible assets and their impact on the valuation of the real property and plant and equipment assets.

Section 20.5. To comply with the requirement to identify the asset to be valued in IVS 101 Scope of Work, para 20.3. (d) the following matters must be included:

(a) a description of the real property interest to be valued,
(b) identification of any superior or subordinate interests that affect the interest to be valued.

Section 20.6. To comply with the requirements to state the extent of the investigation and the nature and source of the information to be relied upon in IVS 101 Scope of Work, para 20.3.(j) and IVS 102 Investigations and Compliance, the following matters must be considered:
(a) the evidence required to verify the real property interest and any relevant related interests.
(b) the extent of any inspection
(c) responsibility for information on the site area and any building floor areas
(d) responsibility for confirming the specification and condition of any building
(e) the extent of investigation into the nature, specification and adequacy of services
(f) the existence of any information on ground and foundation conditions
(g) responsibility for the identification of actual or potential environmental risks
(h) legal permissions or restrictions on the use of the property and any buildings, as well as any expected or potential changes to legal permissions and restrictions.

Section 20.7. Typical examples of special assumptions that may need to be agreed and confirmed in order to comply with IVS 101 Scope of Work, para 20.3. (k) include:
(a) that a defined physical change had occurred, eg, a proposed building is valued as if complete at the valuation date,
(b) that there had been a change in the status of the property, eg, a vacant building had been leased or a leased building had become vacant at the valuation date,
(c) that the interest is being valued without taking into account other existing interests,
(d) that the property is free from contamination or other environmental risks.

Section 20.8. Valuations of real property interests are often required for different purposes including secured lending, sales and purchases, taxation, litigation, compensation, insolvency proceedings and financial reporting.

Section 30. Bases of Value
Section 30.1. In accordance with IVS 104 Bases of Value, a valuer must select the appropriate basis(es) of value when valuing real property interests.

Section 30.2. Under most bases of value, a valuer must consider the highest and best use of the real property, which may differ from its current use (see IVS 104 Bases of Value, para 30.3). This assessment is particularly important to real property interests which can be changed from one use to another or that have development potential.

Section 40. Valuation Approaches and Methods

Section 40.1. The three valuation approaches described in the IVS 105 Valuation Approaches and Methods can all be applicable for the valuation of a real property interest.

Section 40.2. When selecting an approach and method, in addition to the requirements of this standard, a valuer must follow the requirements of IVS 105 Valuation Approaches and Methods, including para 10.3 and 10.4.

Section 50. Market Approach

Section 50.1. Property interests are generally heterogeneous (ie, with different characteristics). Even if the land and buildings have identical physical characteristics to others being exchanged in the market, the location will be different. Notwithstanding these dissimilarities, the market approach is commonly applied for the valuation of real property interests.

Section 50.2. In order to compare the subject of the valuation with the price of other real property interests, valuers should adopt generally accepted and appropriate units of comparison that are considered by participants, dependent upon the type of asset being valued.

Section 50.3. A unit of comparison is only useful when it is consistently selected and applied to the subject property and the comparable properties in each analysis. To the extent possible, any unit of comparison used should be one commonly used by participants in the relevant market.

Section 50.4. The reliance that can be applied to any comparable price data in the valuation process is determined by comparing various characteristics of the property and transaction from which the data was derived with the property being valued. Differences between the

following should be considered in accordance with IVS 105 Valuation Approaches and Methods, para 30.8.

Specific differences that should be considered in valuing real property interests include, but are not limited to:

(a) the type of interest providing the price evidence and the type of interest being valued,

(b) the respective locations,

(c) the respective quality of the land or the age and specification of the buildings,

(d) the permitted use or zoning at each property,

(e) the circumstances under which the price was determined and the basis of value required,

(f) the effective date of the price evidence and the valuation date, and

(g) market conditions at the time of the relevant transactions and how they differ from conditions at the valuation date.

Section 60. Income Approach

Section 60.1. Various methods are used to indicate value under the general heading of the income approach, all of which share the common characteristic that the value is based upon an actual or estimated income that either is, or could be, generated by an owner of the interest.

In the case of an investment property, that income could be in the form of rent (see paras 90.1-90.3); in an owner-occupied building, it could be an assumed rent (or rent saved) based on what it would cost the owner to lease equivalent space.

RATE OF LEASE AMOUNT:

The lease amount payable by the LESSEE to the LESSOR for the Schedule Premises with all Infrastructures shall be based on the Sales Turnover. The Lease amount shall be 11% of Sales Turnover (The turnover clearly mean by NET SALES before tax and Levis excluding the free bills, cancellation bills, Special discount on bills.)

Section 60.2. For some real property interests, the income-generating ability of the property is closely tied to a particular use or business/trading activity (for example, hotels, golf courses, etc). Where a building is suitable for only a particular type of trading activity, the income is often related to the actual or potential cash flows that would accrue to the owner of that building from the trading activity. **The use of a property's trading potential to indicate its value is often referred to as the "profits method".**

Section 60.3. When the income used in the income approach represents cash flow from a business/trading activity (rather than cash flow related to rent, maintenance and other real property-specific costs), the valuer should also comply as appropriate with the requirements of IVS 200 Business and Business Interests and, where applicable, IVS 210 Intangible Assets.

Section 60.4. For real property interests, various forms of discounted cash flow models may be used. The sum of the present-day values for the individual periods represents an estimate of the capital value.
The discount rate in a discounted cash flow model will be based on the time cost of money and the risks and rewards of the income stream in question.

Section 60.5. Further information on the derivation of discount rates is included in IVS 105 Valuation Approaches and Methods, paras 50.29-50.31. The development of a yield or discount rate should be influenced by the objective of the valuation. For example:
(a) if the objective of the valuation is to establish the value to a particular owner or potential owner based on their own investment criteria, the rate used may reflect their required rate of return or their **weighted average cost of capital**, and
(b) if the objective of the valuation is to establish the market value, the discount rate may be derived from observation of the **returns implicit in the price paid for real property interests traded in the market between participants or from hypothetical participants' required rates or return**.

Section 60.6. An appropriate **discount rate may also be built up from a typical "risk-free "return adjusted for the additional risks and opportunities specific to the particular real property interest.**

Section 70. Cost Approach

Section 70.1. In applying the cost approach, valuers must follow the guidance contained in IVS 105 Valuation Approaches and Methods, paras 70.1-70.14.

Section 70.2. This approach is generally applied to the valuation of real property interests through the depreciated replacement cost method.

Section 70.3. It may be used as the primary approach when there is either no evidence of transaction prices for similar property or no identifiable actual or notional income stream that would accrue to the owner of the relevant interest.

Section 70.4. In some cases, even when evidence of market transaction prices or an identifiable income stream is available, the cost approach may be used as a secondary or corroborating approach.

Section 70.6. The cost of the modern equivalent must then, as appropriate, be subject to adjustment for physical, functional, technological and economic obsolescence. The objective of an adjustment for obsolescence is to estimate how much less valuable the subject property might, or would be, to a potential buyer than the modern equivalent. Obsolescence considers the physical condition, functionality and economic utility of the subject property compared to the modern equivalent.

Section 80. Special Considerations for Real Property Interests

Section 80.1. The following sections address a non-exhaustive list of topics relevant to the valuation of real property interests.

(a) Hierarchy of Interests (section 90)

(b) Rent (section 100).

Section 90. Hierarchy of Interests

Section 90.1. The different types of real property interests are not mutually exclusive.

For example, a superior interest may be subject to one or more subordinate interests. The owner of the absolute interest may grant a lease interest in respect of part or all of his interest. Lease interests granted directly by the owner of the absolute interest are “head lease” interests.

Section 90.2. These property interests will have their own characteristics, as illustrated in the following examples:

(a) Although an absolute interest provides outright ownership in perpetuity, it may be subject to the effect of subordinate interests. - Mortgage, lease, easement or restrictions imposed by a previous owner or restrictions imposed by statute

(b) A mortgage, lease, easement interest will be for a defined period, at the end of which the property reverts to the holder of the superior interest out of which it was created and will normally impose obligations on the lessee, eg, the payment of rent and other expenses.

Section 90.3. When valuing a real property interest, it is necessary to identify the rights accruing to the holder of that interest and reflect any constraints or encumbrances imposed by the existence of other interests in the same property.

Section 100. Rent

Section 100.1. Market rent is addressed as a basis of value in IVS 104 Bases of Value.

Section 100.2. When valuing either a superior interest that is subject to a lease or an interest created by a lease, valuers must consider the contract rent and, in cases where it is different, the **market rent**.

Section 100.3. The **contract rent** is the rent payable under the terms of an actual lease. It may be fixed for the duration of the lease or variable. The frequency and basis of calculating variations in the rent will be set out in the lease and must be identified and understood in order to establish the total benefits accruing to the lessor and the liability of the lessee.

* * *

ASSET STANDARDS

3.2. IVS 410 DEVELOPMENT PROPERTY

Section 10.1. The principles contained in the General Standards IVS 101 to IVS 105 apply to valuations of development property. This standard only includes modifications, additional requirements or specific examples of how the General Standards apply for valuations to which this standard applies. Valuations of development property must also follow IVS 400 Real Property Interests.

Section 20. Introduction

Section 20.1. In the context of this standard, development properties are defined as interests where redevelopment is required to achieve the highest and best use, or where improvements are either being contemplated / in progress at the valuation date and include:

(a) the construction of buildings,

(b) previously undeveloped land which is being provided with infrastructure,

(c) the redevelopment of previously developed land,

(d) the improvement or alteration of existing buildings or structures,

(e) land allocated for development in a statutory plan, and

(f) land allocated for a higher value uses or higher density in a statutory plan.

Section 20.2. Valuations of development property may be required for different purposes. It is the valuer's responsibility to understand the purpose of a valuation.

(a) proposed **projects are financially feasible**

(b) in **acquisition and loan security**

(c) **taxation analyses**

(d) **for litigation** requiring valuation analysis

(e) for financial reporting purposes, valuation is required for accounting purpose, **asset acquisitions and sales**, and impairment analysis, and

(f) for **compulsory purchases**.

Section 20.4. The residual value or land value of a development property can be very sensitive to changes in assumptions or projections concerning the income or revenue to be derived from the completed project or any of the development costs that will be incurred.

Section 20.5. This sensitivity also applies to the impact of significant changes in either the costs of the project or the value on completion. of the current value.
If the valuation is required for a purpose where significant changes in value over the duration of a construction project may be of concern to the user (eg, where the valuation is for loan security or to establish a project's viability), the valuer must highlight the potentially disproportionate effect of possible changes in either the construction costs or end value on the profitability of the project and the value of the partially completed property. A sensitivity analysis may be useful for this purpose provided it is accompanied by a suitable explanation.

Section 30. Bases of Value

Section 30.1. In accordance with IVS 104 Bases of Value, a valuer must select the appropriate basis(es) of value when valuing development property.

Section 30.2. The valuation of development property often includes a significant number of assumptions and special assumptions regarding the condition or status of the project when complete. **For example, special assumptions may be made that the development has been completed or that the property is fully leased Property**

Section 30.4. In situations where there has been a change in the market since a project was originally conceived, a project under construction may no longer represent the highest and best use of the land. In such cases, the costs to complete the project originally proposed may be irrelevant as a buyer in the market would either demolish any partially completed structures or adapt them for an alternative project. The value of the development property under construction would need to reflect the current value of the alternative project and the costs and risks associated with completing that project.

Section 40. Valuation Approaches and Methods

Section 40.1. The three principal valuation approaches described in IVS 105 Valuation Approaches and Methods may all be applicable for the valuation of a real property interest. There are two main approaches in relation to the valuation of the development property. These are:

(a) the market approach (see section 50), and

(b) **the residual method, which is a hybrid of the market approach, the income approach and the cost approach** (see sections 40-70).

Section 50. Market Approach

Section 50.3. For development property where work on the improvements has commenced but is incomplete, the application of the market approach is even more problematic.
Such properties are rarely transferred between participants in their partially-completed state, except as either part of a transfer of the owning entity or where the seller is either insolvent or facing insolvency and therefore unable to complete the project. Even in the unlikely event of there being evidence of a transfer of another partially-completed development property closes to the valuation date, the degree to which work has been completed would almost certainly differ, even if the properties were otherwise similar.

Section 50.4. The market approach may also be appropriate for establishing the value of a completed property as one of the inputs required under the residual method, which is explained more fully in the section on the residual method (section 90).

Section 60. Income Approach

Section 60.1. Establishing the residual value of a development property may involve the use of a cash flow model in some markets.

Section 60.2. The income approach may also be appropriate for establishing the value of a completed property as one of the inputs required under the residual method, which is explained more fully in the section on the residual method (see section 90).

Section 70. Cost Approach

Section 70.1. Establishing the development costs is a key component of the residual approach (see para 90.5).

Section 70.2. The cost approach may also exclusively be used as a means of indicating the value of development property such as a proposed development of a building or other structure for which there is no active market on completion.

Section 80. Special Considerations for a Development Property

Section 80.1. The following sections address a non-exhaustive list of topics relevant to the valuation of development property:

(a) Residual Method (section 90).

(b) Existing Asset (section 100).

(c) Special Considerations for Financial Reporting (section 110).

(d) Special Considerations for Secured Lending (section 120).

Section 90. Residual Method

Section 90.1. The residual method is so called because it indicates the residual amount after deducting all known or anticipated costs required to complete the development from the anticipated value of the project when completed after consideration of the risks associated with completion of the project. This is known as the residual value.

Note: This method is an indirect manner of deriving land rate from sale transactions or the land value is derived in an indirect manner.

If a property is fully developed or under-utilized or of inferior use, to get best and high use, and where there is no prior sale instances available

(Eg: commercial / industrial / non-availability of plots sales - there may not be many sale instances available) for a direct comparison, to find out the land rate, these types of residual techniques are used.

In cases, where sales of developed properties available, this indirect method provides the probable land value in the locality.

In cases, where residential apartment's composite rates are available, this residual technique can be adopted to find out the rate for land component.

For apartments, the outgoings towards promoter's profit, architect fees, interest components, plan approval charges, FSI stipulations, development charges, etc. have to be ascertained.

Hypothetical building scheme

By adopting a hypothetical building to be proposed in the property, the sale value of the proposed flats / shops can be derived.

The sale value will be inclusive of profits, interest components, construction cost, outgoings, and management expenses for implementation of the project, etc. After adjustments the net proceeds will be taken as hypothetical building cost.

The land component can be determined from the sale proceeds after deducting the hypothetical building cost.

In case of properties are considered for redevelopment as shopping/ office/ malls and others subject to assumption of rental income or profit, this method can be adopted both by income and cost approach method.

Profitability of development project is based on the Probable rental income receivable from redeveloping the property.

Same can be reviewed, if it is a tenanted or leasehold property, then the land is arrived with the help of income approach method.

Hypothetical Plotting Scheme

This method of valuation of large extent of land is adopted in the following situations.

(a) When the comparable sales of large tracts are not available but sales of small plot are available.

(b) When the land is ripe for use for building purpose it possesses necessary potentialities for urban use.

The complete procedure to determine the fair market value of the large tracts of land, under this method can divided into the following steps.

1. Ascertain the demand for small plots in the area.

2. Determine the area of land required for development work as per municipal bye laws. Deduct this area from the total area of the plot so as to ascertain the area available for development of small size plots with suitable deduction by rough estimation on the total area.

3. Determine the number of small plots which can be legally made out from the large tract of land with necessary provisions for infrastructure facilities.

4. Determine the cost of development works such as cost in of construction of road as per municipal specifications with street lights, cost of laying parks, underground drains, water supply lines, sewer lines, electric lines & substation, earth fitting or cutting, cross drainage works and municipal taxes on open land.

As the total amount of development is not paid to the contractor at the commence mend of work so defer it for half of the period of construction at certain rate of interest say to 12%. Let the deferred value be (A).

5. Ascertain the total sale price of all the small plots of scheme on the valuation date from the comparable sales of small developed plots.

As all these small plots cannot be sold at one time, so estimate the time of disposal of all the plots and defer the total sale price for half of the period of the sale @ 10% to 12%. Let it be of (B).

6. From the deferred sale price (B) deduct the following.

(i) Present value of the cost of development deferred for 1/4th or 1/3rd or half of the period of development (A) along with architect or engineers fee for his supervision and getting the scheme approved.
(ii) Incidental charges such as cost of stamps, registration legal cost, cost of advertisement etc. Normally it is 10% to 20% of (B). If the cost of stamp, registration and legal cost is to be borne by the purchaser then this percentage should be modifier accordingly.
(iii) Developer's profit and risk 15% of (B).
7. This amount available after above deductions from (B) will represent the fair market value of the large undeveloped plot on the date of valuation.

Section 90.2. The residual value can be highly sensitive to relatively small changes in the forecast cash flows and the practitioner should provide separate sensitivity analyses for each significant factor.

Section 90.5. In applying the residual method, a valuer should consider and evaluate the reasonableness and reliability of the following:
(a) the source of information on any proposed building or structure, eg, any plans and specification that are to be relied on in the valuation, and
(b) any source of information on the construction and other costs that will be incurred in completing the project and which will be used in the valuation.

Section 90.6. The following basic elements require consideration in any application of the method to estimate the market value of development property and if another basis is required, alternative inputs may be required.
(a) Completed property value
(b) Construction costs
(c) Consultants fees
(d) Marketing costs
(e) Timetable
(f) Finance costs
(g) Development profit,
(h) Discount rate.

Value of Completed Property - Analysis of Project report – Check list

Section 90.7. Estimate of the value of the relevant interest in the real property following **notional completion of the development project**

Section 90.8. Methods adopted under either the market or income approach

(a) the estimated market value on completion is based on values that are current on the valuation date on the special assumption the project had already been completed in accordance with the defined plans and specification, or

(b) the estimated value on completion is based on the special assumption that the project is completed in accordance with the defined plans and specification on the anticipated date of completion.

Section 90.9. Market practice and availability of relevant data should determine which of these assumptions is more appropriate.

Section 90.11. Ensure that consistent assumptions are used throughout the residual value calculation,

ie, **if current values are used then the costs should also be current and discount rates derived from analysis of current prices**.

Section 90.12. If there is a pre-sale or pre-lease agreement in place that is conditional on the project, or a relevant part, being completed, this will be reflected in the valuation of the completed property.

Establish whether the price in a pre-sale agreement or the rent and other terms in a pre-lease agreement reflect those that would be agreed between participants on the valuation date.

Section 90.13. If the terms are not reflective of the market, adjustments need to be made

Construction Costs

Section 90.15. The costs of all work required at the valuation date to complete the project to the defined specification to be identified.

Where no work has started, this will include any preparatory work required prior to the main building contract, such as the costs of obtaining statutory permissions, demolition or off-site enabling work.

Section 90.16. Where work has commenced, or is about to commence, there will normally be a contract or contracts in place that can provide the independent confirmation of cost. However, if there are no contracts in place, or if the actual contract costs are not typical of those that would be agreed in the market, then it is necessary to estimate these costs reflecting the reasonable expectation of participants on the valuation date of the probable costs.

Section 90.19. However, contractual costs may include special requirements of a specific end user and therefore may not reflect the general requirements of participants.

Consultants' Fees

Section 90.23. These include legal and professional costs that would be reasonably incurred by a participant at various stages through the completion of the project.

Marketing Costs

Section 90.24. If there is no identified buyer or lessee for the completed project, it will normally be appropriate to allow for the costs associated with appropriate marketing, and for any leasing commissions and consultants' fees incurred for marketing not included

Timetable

Section 90.25. The duration of the project from the valuation date to the expected date of physical completion of the project to be considered, together with all cash outflows for construction costs, consultants' fees,

Section 90.26. If there is no sale agreement after completion, an estimate should be made of the marketing period that might typically be required until a sale is achieved.

Section 90.27. If the property is to be held for investment after completion and if there are no pre-leasing agreements, the time required to reach stabilised occupancy needs to be considered (ie, the period required to reach a realistic long-term occupancy level).
Allowance should be considered for costs incurred by the owner during this period such as additional marketing costs, incentives, maintenance and/or unrecoverable service charges.

Finance Costs

Section 90.28. These represent the cost of finance for the project from the valuation date through to the completion of the project, including any period required after physical completion to either sell the interest or achieve stabilised occupancy. The finance cost during each period may also need to be considered separately. Even if an entity is intending to self-fund the project, an allowance should be made for interest at a rate which would be obtainable by a participant for borrowing to fund the completion of the project on the valuation date.

Development Profit

Section 90.29. Allowance should be made for development profit, or the return for taking on the risks for completion of the project on the valuation date.

Section 90.30. This target profit can be expressed as a lump sum, a percentage return on the costs incurred or a percentage of the anticipated value of the project on completion or a rate of return.

The amount of profit for the risk will vary according to factors such as:

(a) the stage which the project has reached on the valuation date.

(b) whether a buyer or lessee has been secured for the completed project, and

(c) the size and anticipated remaining duration of the project.

Section 90.31. The following are examples of factors that may typically need to be considered in an assessment of the relative risks associated with the completion of a development project:

(a) unforeseen complications that increase construction costs,

(b) potential for contract delays caused by nature or outside of the developer's control,

(c) delays in obtaining statutory consents,

(d) supplier failures,

(e) entitlement risk and changes in entitlements over the development period,

(f) regulatory changes, and

(g) delays in finding a buyer or lessee for the completed project.

Discount Rate

Section 90.35. the residual method requires the application of a discount rate to all future cash flows in order to arrive at a net present value. This discount rate may be derived using a variety of methods

Section 90.36. If the current cash flows are based on values and costs, the risk between valuation date and anticipated completion date must reflect in the discount rate used to determine the present value

Section 100. Existing Asset

Section 100.1. Check list for valuation of a development property before a project commences:

(a) market potential for the proposed development,
(b) proposed development is HABU in current market,
(c) any non-financial obligations (political or social criteria),
(d) legal permissions or zoning, - conditions or constraints on permitted development,
(e) limitations, encumbrances or conditions imposed
(f) rights of access to public highways or other public areas,
(g) geotechnical conditions, including potential for contamination or other environmental risks,
(h) availability of, or improve needed for services,
(i) the need for any off-site infrastructure improvements and the rights required to undertake this work,
(j) archaeological constraints / archaeological investigations required,
(k) sustainability and client requirements in relation to green buildings,
(l) economic conditions and trends and their potential impact on costs and receipts during the development period,
(m) current / projected supply and demand for proposed future uses,
(n) the availability and cost of funding,
(o) the expected time required to deal with preparatory matters prior to starting work, for the completion of the work and, if appropriate, to rent or sell the completed property,
(p) any other risks associated with the proposed development.

Section 100.2. When project is in progress, need for additional enquires or investigations for design, construction and supervision.

Section 120. Special Considerations for Secured Lending

Section 120.1. The appropriate basis of valuation for secured lending is normally market value. However, in considering the value of a development property, regard should be given to the probability that any contracts in place, eg, for construction or for the sale or

leasing of the completed project may, become void or voidable in the event of one of the parties being the subject of formal insolvency proceedings. Further regard should be given to any contractual obligations that may have a material impact on market value.
Therefore, it may be appropriate to highlight the risk to a lender caused by a prospective buyer of the property not having the benefit of existing building contracts and/or pre-leases, and pre-sales and any associated warrantees and guarantees in the event of a default by the borrower.

Section 120.2. To demonstrate an appreciation of the risks involved in valuing development property for secured lending or other purposes, the valuer should apply a minimum of two appropriate and recognised methods to valuing development property for each valuation project, as this is an area where there is often “insufficient factual or observable inputs for a single method to produce a reliable conclusion”

Section 120.3. The valuer must be able to justify the selection of the valuation approach(es) reported and should provide
an “As Is” (existing stage of development) and
an “As Proposed” (completed development) value for the development property and record the process undertaken and a rationale for the reported value"

Determination of Fair Market Value by Development Method - Hypothetical Plotting Scheme	
Mr X has a vacant land of 40000 sq m within the town limits and wants to develop this vacant land as residential plots layout and sell them in piecemeal basis	
DATA COLLECTION	
Area of Plot	40.000 Sqm.
Area required for layout services and amenities	25% of Plot Area
Average price of small plots in the locality	Rs. 1000/- Sqm
Period of Development	2 years
Cost of development of saleable area	Rs. 45/- Sqm
Period of sale	3 years
Architect fees	2%
Developer's profit	15%

Legal charges, marketing, and others	8%
SOLUTION	
Area of Plot	40.000 Sqm
Deduct land area required for laying services & amenities	10,000 Sqm
Net area available for sale	30,000 Sqm
Cost of land available for sale = 30,000 X Rs 1000 / sqm	Rs. 300 Lakhs (A)
Defer (A) for 1.5 years being @ 50% of total sale period of 3 years @ 12% P.A. = 300 x 0.84503	Rs. 253.51Lakhs (B)
DEDUCTIONS	
Cost of development = 30000 X Rs 45 / sqm = Rs. 13.50 Lakh Deferring it @ 12% P.A. for 1.0 year being the 50% of time period of development = 13.50 X 0.89286	Rs. 12,05,361
Architect fee @ 2% of deferred development cost Rs 1205361 X 2 %	Rs. 24,107
Legal charge, brokerage etc. @ 8% of (B)	Rs. 20,28,0721
Developers profit @ 15% of (B)	Rs. 38,02,635
Total Deductions	Rs. 70,60,175 Say Rs 70.60 lakhs
F.M. V. of the Plot = 253.51 - 70.60	**Rs. 182.91 Lakhs**

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4. Glossary (updated: **March 2020***)*

This Glossary is produced to help promote consistency in the usage of words and terms that are common in valuation assignments of different types. Some of the definitions appear in the International Valuation Standards, in Technical Information Papers or in other IVSC publications, but others commonly occurring words and terms used in valuation practice are included.

The definitions included meet the following criteria:

The Glossary should only include words or terms that either:

- have a meaning when used in a valuation context that either differs from, or is more specific than, their meaning in everyday usage,
- are technical, ie they may not be familiar to a reader who has a reasonable level of business knowledge and sophistication, or that have proved difficult in translation into languages other than English, or
- are definitions used in the International Valuation Standard, a Technical Information Paper or other IVSC publication.
- Definitions should be concise – ideally no more than a short sentence, although there are some exceptions allowed.
- The Glossary should not include words or terms that may be relevant to understanding or describing a particular asset type but that do not directly relate to the valuation process.
- The Glossary should generally avoid accounting or legal definitions unless these are directly relevant to valuation and widely used in valuation practice.
- The Glossary should avoid words or terms that are specific to a particular state when there is a suitable internationally recognized equivalent.
- The Glossary contains only the definition of the word or term, not an explanation of its application in practice.

The definitions in this glossary are those recommended by the IVSC, but other definitions and terms exist. Users of this Glossary are advised to check whether the IVS definition was intended before relying on a definition it contains to interpret any document. The International Valuation Standards Council, the authors and the publishers do not accept responsibility for loss caused to any person who acts or refrains from acting in reliance on the material in this publication, whether such loss is caused by negligence or otherwise.

in the normal course of business or for educational purposes providing the source of the definition is acknowledged as the IVSC. Otherwise the Glossary is subject to the **terms of use** of this website.

The IVSC keeps this Glossary under review and any updates are made on 1 January and 1 July each year. It welcomes suggestions for either additional definitions or amendments to an existing definition. If suggesting a new definition please have regard to the criteria noted above. The final decision on whether to accept a recommendation rest with the IVSC Standards Board. The IVSC cannot enter into correspondence over any decisions made in respect of this Glossary.

A

All Risks Yield

The reciprocal of the Capitalization Factor, usually expressed as a percentage. See also: Capitalization Factor; Capitalization Rate; Reversionary Yield: Yield; Yield to Maturity

Annuity

A series of annual payments made or received at intervals either for life or for a fixed number of periods.

Appraisal

Arbitrage Pricing Theory. A multivariate model for estimating the cost of equity capital, which incorporates several systematic risk factors.

Asset or Assets

To assist in the readability of the standards and to avoid repetition, the words "*asset*" and "*assets*" refer generally to items that might be subject to a valuation engagement. Unless otherwise specified in the standard, these terms can be considered to mean "*asset, group of assets, liability, group of liabilities, or group of assets and liabilities*". (IVS page 3)

Assumed Use

A Premise of Value or Assumed Use describes the circumstances of how an asset or liability is used. (IVS 104 p24 120.1)

Asset Based Approach

A method of indicating the value of a business, business or business interest based on a summation of the net value of the individual assets and liabilities. Since each of the assets and liabilities will have been valued using either the market, income or cost approaches, it is not a distinct valuation approach.

B

Basis of Value

A statement of the fundamental measurement assumptions of a valuation.

Beta

A measure of systemic risk of a stock; the tendency of a stock's price to correlate with changes in a specific index.

Blockage Discount

An amount or percentage that would be deducted by market participants from the current market price of a publicly traded stock to reflect the decrease in the value per share of a block of stock that is of a size that could not be sold in a reasonable period of time given normal trading volumes.

Book Value

See: Carrying Amount

Business (Business Enterprise)

A commercial, industrial, service, or investment entity (or a combination thereof) pursuing an economic activity.

Business Risk

The degree of uncertainty of realizing expected future returns of the business resulting from factors other than financial leverage. See also: Financial Risk; Market Risk; Systematic Risk

C

Capital Asset Pricing Model (CAPM)

A model in which the cost of capital for any stock or portfolio of stocks equals a risk-free rate plus a risk premium that is proportionate to the systematic risk of the stock or portfolio.

Capital Structure

The composition of the invested capital of a business enterprise; the mix of debt and equity financing.

Capitalization

1. the conversion of a periodic income to an equivalent capital value,
2. the Capital Structure of a business entity, or
3. the recognition of expenditure in a Financial Statement as a capital asset rather than a periodic expense.

Capitalization Factor

The multiple applied to a representative single period income to convert it into a capital value. See also: All Risks Yield; Capitalization Rate; Yield;

Capitalization Rate

The return represented by the income produced by an investment, expressed as a percentage. See also: All Risks Yield; Capitalization Factor; Yield;

Carrying Amount

The amount at which an asset is recognized in the financial statements of an entity after deducting any accumulated depreciation and any accumulated impairment losses. See also: Book Value

Cash Flow

Cash that is generated over a period of time by an asset, group of assets, or business enterprise. Usually used with a qualifying word or phrase. See also: Free Cash Flows to Equity, Free Cash Flows to the Firm, Nominal Cash Flows, Real Cash Flows

Client

The word "*client*" refers to the person, persons, or entity for whom the valuation is performed. This may include external clients (i.e., when a valuer is engaged by a third-party client) as well as internal clients (i.e., valuations performed for an employer). (IVS page)

Cost Approach

The cost approach provides an indication of value using the economic principle that a buyer will pay no more for an asset than the cost to obtain an asset of equal utility, whether by purchase or by construction, unless undue time, inconvenience, risk or other factors are involved. (IVS 105 p44 60.1)

Contract Rent

The rent specified in a lease. May differ from the market rent. See also: Market Rent

Contributory Asset Charges

A charge to reflect a fair return on or return of Contributory Assets used in the generation of the cash flows associated with the intangible asset being valued. See also: Contributory Assets, Excess Earnings Method, Multi Period Excess Earnings Method

Contributory Assets

Any tangible or intangible assets used in the generation of the cash flows associated with the intangible asset being valued. See also: Contributory Asset Charges

Control Premium

An amount or a percentage by which the pro rata value of a controlling interest exceeds the pro rata value of a non-controlling interest in a business enterprise, to reflect the power of control.

Cost Approach

A valuation approach based on the economic principle that a buyer will pay no more for an asset than the cost to obtain an asset of equal utility, whether by purchase or by construction.

Cost of Capital

The expected rate of return that the market requires in order to attract funds to a particular investment.

Credit Risk

The risk that one party to a contract will cause a financial loss for the other by failing to discharge an obligation.

Current Assets

Cash and assets that are reasonably expected to be converted into cash within one year in the normal course of business. See also: Current Liabilities

Current Liabilities

Debts or obligations that are due within one year. See also: Current Assets

D

Default Probability

The likelihood of a counterparty not honouring its obligations.

Depreciated Replacement Cost Method

A method under the cost approach that indicates value by calculating the current replacement cost of an asset less deductions for physical deterioration and all relevant forms of obsolescence. See also: Cost Approach; Economic Obsolescence; Functional Obsolescence;

Discount for Lack of Control

An amount or percentage deducted from a pro-rata share of the value of 100 percent of an equity interest in a business, to reflect the absence of some or all of the powers of control. See also: Control Premium.

Discount Rate

A rate of return used to convert a future monetary sum or cash flow into present value.

Discounted Cash Flow Method

A method within the income approach in which a discount rate is applied to future expected income streams to estimate the present value.

E

Economic Life

The total period of time over which an asset is expected to generate economic benefits for one or more users See also: Useful Life

Economic Obsolescence

A loss of utility caused by factors external to the asset, especially factors related to changes in supply or demand for products produced by the asset, that results in a loss of value.
See also: External Obsolescence, ; Functional Obsolescence,; Physical Obsolescence

Enterprise Value

The total value of the equity in a business plus the value of its debt or debt-related liabilities, minus any cash or cash equivalents available to meet those liabilities. See also: Invested Capital

Entity Specific Factors

Factors that are specific to an entity and not available to market participants generally.

Equity

The owner's interest in an asset or business after deduction of all liabilities.

Equitable Value

The estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties. (IVS 104 p21 50.1)

Equity Instrument

Any contract that creates a residual interest in the assets of an entity after deducting all of its liabilities.

Equity Risk Premium

A rate of return added to a risk-free rate to reflect the additional risk of equity instruments over risk free instruments (a component of the cost of equity capital or equity discount rate).

Equity Value

The value of a business to all of its shareholders

Excess Earnings

That amount of anticipated economic benefits that exceeds an appropriate rate of return on the value of a selected asset base (often net tangible assets) used to generate those anticipated economic benefits.

Excess Earnings Method

A method of estimating the economic benefits of an intangible asset by identifying the cash flows associated with the use of the asset and deducting a charge reflecting a fair return for the use of contributory assets.

See also: Contributory Asset Charges, Greenfield Method, Multi Period Excess Earnings Method

Expected Negative Exposure

The discounted payments and unrealized losses an entity expects to pay to a counterparty.

Expected Positive Exposure

The discounted receipts and unrealized gains an entity forecasts will be received from a counterparty

External Obsolescence

A loss of utility caused by economic or locational factors external to the asset that results in a loss of value.

See also: Economic Obsolescence, Functional Obsolescence, Obsolescence, Physical Obsolescence.

External Valuer

A valuer who is not employed by the owner or manager of an asset.

F

Fair Value

1. The estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties.

For use in financial reporting under International Financial Reporting Standards, fair value has a different meaning: ii. In IFRS 13 “Fair Value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.”

2. The distinction between these two definitions and their usage is discussed in the IVS Framework paras 39-43 and IVS 300, paras G1-G2

Fair Market Value (OECD)

The price a willing buyer would pay a willing seller in a transaction on the open market. (IVS 104 p23 100.1)

Fair Market Value (US IRS)

The fair market value is the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts. (IVS 104 p23 110.1)

Fair Value (IFRS 13/ US ASC 820)

The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. (IVS 104 p23 90.1)

Forced Sale

Circumstances where a seller is under compulsion to sell and that, as a consequence, a proper marketing period is not possible, and buyers may not be able to undertake adequate due diligence. (IVS 104 p25 170.1)

Fairness Opinion

An opinion on whether the financial terms of a proposed corporate transaction are fair to the equity holders of an entity involved.

Financial Instrument

A contract that creates rights or obligations between specified parties to receive or pay cash or other financial consideration, or an equity instrument.

Financial Reporting Standards

Any recognized or adopted standards for the preparation of periodic statements of an entity's financial position. These may also be referred to as accounting standards.

See also: International Financial Reporting Standards

Financial Risk

The degree of uncertainty of realizing expected future returns of the business resulting from financial leverage. See also: Business Risk; Market Risk; Systematic Risk.

Financial Statement

A periodic statement of an entity's financial position

Free Cash Flows to Equity

Cash flows available to pay out to equity owners after funding operations of the business, making necessary capital investments, and increasing or decreasing debt financing. See also: Free Cash Flows to the Firm

Free Cash Flows to the Firm

Cash flows available to pay out to equity holders and debt investors after funding operations of the business enterprise and making necessary capital investments. See also: Free Cash Flows to Equity.

Functional Obsolescence

A loss of utility resulting from inefficiencies in the subject asset compared to its replacement that results in a loss of value. See also: Economic Obsolescence; External Obsolescence; Obsolescence; Physical Obsolescence

G

Going Concern

A business enterprise that is expected to continue operations for the foreseeable future.

Goodwill

Any future economic benefit arising from a business, an interest in a business or from the use of a group of assets which is not separable.

Greenfield Method

A method of valuing an intangible asset that deducts the cost of buying or creating contributory assets from the cash flows associated with the use of that asset. See also: Contributory Assets; Excess Earnings Method, Multi Period Excess Earnings Method

H

Highest and Best Use

The use of an asset that maximizes its potential and that is physically possible, legally permissible and financially feasible.

I

Impairment

A loss in the future economic benefits, or service potential of an asset, over and above the systematic recognition of the loss of the asset's future economic benefits or service potential through depreciation or amortization.

Intended Use

The use(s) of a valuer's reported valuation or valuation review results, as identified by the valuer based on communication with the client. (IVS page 3)

Intended User

The client and any other party as identified, by name or type, as users of the valuation or valuation review report by the valuer based on communication with the client. (IVS page 3)

Investment Value/Worth

The value of an asset to a particular owner or prospective owner for individual investment or operational objectives. (IVS 104 p22 60.1)

Income Approach

A valuation approach that provides an indication of value by converting future cash flows to a single current capital value.

Initial Yield

The initial income from an investment divided by the price paid for the investment expressed as a percentage. See also: All Risks Yield; Reversionary Yield; Yield; Yield to Maturity

Intangible Asset

A non-monetary asset that manifests itself by its economic properties. It does not have physical substance but grants rights and economic benefits to its owner.

Internal Rate of Return

The discount rate at which the present value of the future cash flows of the investment equals the acquisition cost of the investment.

International Financial Reporting Standards

Standards and interpretations adopted by the International Accounting Standards Board (IASB). They comprise:

- International Financial Reporting Standards,
- International Accounting Standards, and
- Interpretations developed by the International Financial Reporting Interpretations Committee (IFRIC) or the former Standing Interpretations Committee (SIC)

Invested Capital

The sum of equity and debt in a business enterprise. Debt can be either (a) all interest-bearing debt or (b) long-term, interest-bearing debt. When the term is used, it should be supplemented by the appropriate qualifying words. See also: Enterprise Value

Investment Method

A valuation method under the Income Approach that capitalizes expected future income or utility as a basis for estimating value.

Investment Property

Property that is land or a building, or part of a building, or both, held by the owner to earn rentals or for capital appreciation, or both, rather than for:

1. use in the production or supply of goods or services or for administrative purposes,
2. sale in the ordinary course of business.

Investment Value

The value of an asset to the owner or a prospective owner for individual investment or operational objectives.

J

Jurisdiction

The word "*jurisdiction*" refers to the legal and regulatory environment in which a valuation engagement is performed. This generally includes laws and regulations set by governments (eg, country, state and municipal) and, depending on the purpose, rules set by certain regulators (eg, banking authorities and securities regulators). (IVS page 3)

L

Lease

An agreement whereby a lessor grants the right to use an asset for an agreed period of time to a lessee in return for a payment or series of payments. See also: Lessee, Lessor.

Lessee

A person or corporate entity to entitled to use an asset under the terms of a lease. See also: Lease, Lessor.

Lessor

A person or corporate entity that grants another the rights to use an asset under the terms of a Lease in return for the receipt of a payment or series of payments. See also: Lease, Lessee

Levered Beta

The beta reflecting a capital structure that includes debt. See also: Beta

Liquidation Value

The net amount that would be realized if a business is discontinued and its assets are sold individually. The amount that would be realized when an asset or group of assets are sold on a piecemeal basis. (IVS 104 p22 80.1) The appropriate bases of value and any appropriate additional qualifying assumptions should also be stated.

Liquidity

A measure of the ease with which an asset may be converted into cash. A highly liquid asset can be easily converted into cash; an illiquid asset is difficult to convert into cash.

Loss Given Default

The percentage amount that a party expects to lose if the counterparty defaults

M

Majority Control

The degree of control provided by a majority position.

Majority Interest

An ownership interest greater than 50% of the voting interest in a business enterprise.

Market Approach

A valuation approach which provides an indication of value by comparing the subject asset with identical or similar assets for which price information is available. The market approach provides an indication of value by comparing the asset with identical or comparable (that is similar) assets for which price information is available. (IVS 105 p30 20.1)

Market Participants

The whole body of individuals, companies or other entities that are involved in actual transactions or who are contemplating entering into a transaction for a particular type of asset.

Market Rent

Market Rent is the estimated amount for which an interest in real property should be leased on the valuation date between a willing lessor and a willing lessee on appropriate lease terms in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion. (IVS 104 p21 40.1)

Market Risk

Risk that affects an entire market and not just specific participants or assets. Market Risk cannot be diversified. See also: Business Risk, Financial Risk, Systematic Risk; Systemic Risk; Unsystematic Risk.

Market Value

The estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion. (IVS 104 p18 30.1)

Minority Discount

A discount for lack of control applicable to a minority interest.

Minority Interest

An ownership interest less than 50% of the voting interest in a business enterprise.

Modern Equivalent Asset

An asset which provides similar function and equivalent utility to the asset being valued, but which is of a current design and constructed or made using current materials and techniques.

Multi-Period Excess Earnings Method

A method of estimating the economic benefits of an intangible asset over multiple time periods by identifying the cash flows associated with the use of the asset and deducting a periodic charge reflecting a fair return for the use of contributory assets. See also: Contributory Assets; Contributory Asset Charges; Excess Earnings Method; Greenfield Method.

May

The word "*may*" describes actions and procedures that valuers have a responsibility to consider. Matters described in this fashion require the valuer's attention and understanding. How and whether the valuer implements these matters in the valuation engagement will depend on the exercise of professional judgement in the circumstances consistent with the objectives of the standards. (IVS page 3)

Must

The word "*must*" indicates an unconditional responsibility. The valuer must fulfill responsibilities of this type in all cases in which the circumstances exist to which the requirement applies. (IVS page 3)

N

Net Book Value

1. In relation to a business enterprise: The difference between total assets (net of accumulated depreciation, depletion, and amortization) and total liabilities as they appear on the balance sheet.

2. In relation to a specific asset: The capitalized cost less accumulated amortization or depreciation as it appears on the books of account of the business enterprise. See also: Book Value, Carrying Amount.

Net Present Value

The value, as of a specified date, of future cash inflows less all cash outflows (including the cost of investment) calculated using an appropriate discount rate. See also: Present Value

Nominal Cash Flows

Cash flows expressed in monetary terms in a given period or series or periods.

Non-Current Assets

Assets that are held long term and intended for use by an enterprise in the production of goods or the delivery of services. See also: Current Assets

Non-operating Assets

Classes of assets that are not essential to the operations of a business, but may still generate income or provide return on investment.

Normalized Earnings

Economic benefits adjusted for non-recurring, non-economic, or other unusual items to facilitate comparisons.

O

Obsolescence

A loss of utility of an asset caused by either physical deterioration, changes in technology, patterns of demand or environmental changes that results in a loss of value. See also: Economic Obsolescence; External Obsolescence; Functional Obsolescence; Physical Obsolescence.

P

Physical Obsolescence

A loss of utility due to the physical deterioration of the asset or its components resulting from its age and normal usage that results in a loss of value.

Plant and Equipment

A class of tangible asset that is:

1. held by an entity for use in the production or supply of goods or services, for rental by others or for administrative purposes and
2. expected to be used over a period of time.

Plant and Machinery

See Plant and Equipment

Portfolio

An assemblage of various assets or liabilities held or managed by a single entity.

Premium Profits Method

A method that indicates the value of an intangible asset by comparing an estimate of the profits or cash flows that would be earned by a business using the asset with those that would be earned by a business that does not use the asset.

Present Value

The value, as of a specified date, of a future payment or series of future payments discounted to the specified date (or to time period zero) at an appropriate discount rate. See also: Net Present Value.

Price / Earnings Ratio

The price of a share of stock divided by its earnings per share.

Prospective Financial Information

Forecast financial data used to estimate cash flows in a discounted cash flow model.

Participant

The word "*participant*" refers to the relevant participants pursuant to the basis (or bases) of value used in a valuation engagement (see IVS 104 Bases of Value). Different bases of value require valuers to consider different perspectives, such as those of "market participants" (eg, Market Value, IFRS Fair Value) or a particular owner or prospective buyer (eg, Investment Value). (IVS page 4)

Purpose

The word "*purpose*" refers to the reason(s) a valuation is performed. Common purposes include (but are not limited to) financial reporting, tax reporting, litigation support, transaction support, and to support secured lending decisions. (IVS page 4)

R

Rate of Return

An amount of income (loss) and/or change in value realized or anticipated on an investment, expressed as a percentage of that investment.

Real Cash Flows

Nominal cash flows adjusted to exclude the effect of price changes over time.

Real Estate

Land and all things that are a natural part of the land, eg, trees and minerals, things that have been attached to the land, eg, buildings and site improvements, all permanent building attachments, eg, mechanical and electrical plant providing services to a building, that are both below and above the ground.

Real Property

All rights, interests and benefits related to the ownership of real estate.

Relief from Royalty Method

A method that estimates the value of an intangible asset by reference to the value of the hypothetical royalty payments that are saved through owning the asset, as compared with licensing it from a third party.

See also: Royalty

Replacement Cost

The current cost of a similar asset offering equivalent utility.

See also: Modern Equivalent Asset.

Replication Method

A valuation method under the Cost Approach typically used for valuing financial instruments that provides an indication of the current value of an instrument or portfolio by reproducing or "replicating" its risks and cash flows in a hypothetical, or synthetic, alternative.

Reproduction Cost

The current cost of creating a replica of the asset

Residual Value 1. The anticipated value of an asset at the expiration of its useful life. See also: Salvage Value2. IFRS definition (IAS16): "The estimated amount that an entity would currently obtain from disposal of an asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life." The application of the IFRS definition is described in IVS 300 Valuations for Financial Reporting.

Reversionary Value

The estimated value of an investment property at the end of a period during which the rental income is either above or below the market rent. See also: Terminal Value

Reversionary Yield

The anticipated yield from an Investment Property once the Reversionary Value is attained.

See also: All Risks Yield; Reversionary Value; Yield;

Risk Free Rate

The rate of return available in the market on an investment free of default risk.

Risk Premium

A rate of return added to a risk-free rate to reflect risk.

Royalty

A payment made for the use of an asset, especially an intangible asset or a natural resource. See also: Relief from Royalty Method.

S

Sale and Leaseback

Simultaneous transactions in which the buyer becomes the Lessor and the seller becomes the Lessee. See also: Lessee; Lessor

Salvage Value

The value of an asset that has reached the end of its economic life for the purpose it was made. The asset may still have value for an alternative use or for recycling. See also: Residual Value.

Service Potential

The capacity of an asset to continue to provide goods and services in accordance with the entity's objectives.

Special Assumption

An assumption that either assumes facts that differ from the actual facts existing at the valuation date or that would not be made by a typical market participant in a transaction on the valuation date.

Special Purchaser

A particular buyer for whom a particular asset has special value because of advantages arising from its ownership that would not be available to other buyers in a market.

Special Value

An amount that reflects particular attributes of an asset that are only of value to a special purchaser.

Specialized Property

A property that is rarely if ever sold in the market, except by way of sale of the business or entity of which it is part, due to uniqueness arising from its specialized nature and design, its configuration, size, location or otherwise. See also: Trade Related Property

Summation Method

A valuation method that provides an indication of the value of an entire asset by the addition of the separate values of its component parts. See also: Asset Based Approach.

Synergistic Value

An additional element of value created by the combination of two or more interests where the value of the combined interest is worth more than the sum of the original interests.

Synergistic Value is the result of a combination of two or more assets or interests where the combined value is more than the sum of the separate values. (IVS 104 p22 70.1)

Systematic Risk

Risk that affects an entire market and not just a specific company or asset. Systematic Risk cannot be diversified. See also: Business Risk; Financial Risk; Market Risk; Systemic Risk; Unsystematic Risk.

Should

The word "*should*" indicates responsibilities that are presumptively mandatory. The valuer must comply with requirements of this type unless the valuer demonstrates that alternative actions which were followed under the circumstances were sufficient to achieve the objectives of the standards. In the rare circumstances in which the valuer believes the objectives of the standard can be met by alternative means, the valuer must document why the indicated action was not deemed to be necessary and/or appropriate. If a standard provides that the valuer "*should*" consider an action or procedure, consideration of the action or procedure is presumptively mandatory, while the action or procedure is not. (IVS page 4)

Significant and/or Material

Assessing significance and materiality require professional judgement. However, that judgement should be made in the following context:

- Aspects of a valuation (including inputs, assumptions, special assumptions, and methods and approaches applied) are considered to be significant/material if their application and/or impact on the valuation could reasonably be expected to influence the economic or other decisions of users of the valuation; and judgments about materiality are made in light of the overall valuation engagement and are affected by the size or nature of the subject asset.
- As used in these standards, "material/materiality" refers to materiality to the valuation engagement, which may be different from materiality considerations for other purposes, such as financial statements and their audits. (IVS page 4-5)

Subject or Subject Asset

These terms refer to the asset(s) valued in a particular valuation engagement. (IVS page 5)

T

Tangible Assets

Assets with a physical manifestation. Examples include land and buildings, plant and machinery, fixtures and fittings, tools and equipment, and assets in the course of construction and development.

Tax Amortization Benefit

Tax relief available on amortization of the capitalized asset.

Technical Obsolescence

See Functional Obsolescence.

Terminal Value

The value at the end of an explicit forecast period of all remaining projected cash flows. See also: Reversionary Value

Trade Related Property

Any type of real property designed for a specific type of business where the property value reflects the trading potential for that business. See also: Specialized Property

U

Unit of Account

IFRS Definition (IFRS 13): The level at which an asset or a liability is aggregated or disaggregated in an IFRS for recognition purposes.

The application of the IFRS definition is described in the guidance section of IVS 300 Valuations for Financial Reporting

Unit(s) of Comparison

A common basis of comparison used to analyses differences between assets. It may be based on a physical characteristic, eg a price per square metre or square foot, or an economic characteristic eg the ratio of a asset's sale price to its net income.

Unsystematic Risk

A risk that is specific to a company or asset. Can be diversified. See also: Business Risk; Financial Risk; Market Risk, Systematic Risk; Systemic Risk

Useful Life

IFRS Definition from IAS 16:

(a) the period over which an asset is expected to be available for use by an entity; or

(b) the number of production or similar units expected to be obtained from the asset by an entity. See also: Economic Life

Utility

An expression of the degree of an asset's usefulness.

V

Valuation

A "*valuation"* refers to the act or process of determining an estimate of value of an asset or liability by applying IVS. (IVS page 5)

(1) The process of establishing the value of an asset or liability or

(2) The amount representing an opinion or estimate of value See also: Appraisal

Valuation Approach

One of three principal ways of estimating value. Each valuation approach includes different methods that may be used to apply the principles of the approach to specific asset types or situations. See also: Cost Approach; Income Approach; Market Approach; Valuation Method

Valuation Date

The date on which the opinion of value applies. The valuation date shall also include the time at which it applies if the value of the type of asset can change materially in the course of a single day.

Valuation Inputs

Data and other information that is used in a valuation method. Inputs may be actual or estimated.

Valuation Method

A specific technique or model used to estimate value. All valuation methods fall within a valuation approach. See also: Valuation Approach

Valuation Report

A report that communicates a valuation opinion and relevant associated matters to its intended recipient. The matters to be addressed in a valuation report are set out in IVS 103 Reporting.

Valuation Review

The act or process of considering and reporting on a valuation undertaken by another party, which may or may not require the reviewer to provide their own valuation opinion.

Valuation Reviewer

A “*valuation reviewer*” is a professional valuer engaged to review the work of another valuer. As part of a valuation review, that professional may perform certain valuation procedures and/or provide an opinion of value. (IVS page 5)**Value (n)**

The word “*value*” refers to the judgement of the valuer of the estimated amount consistent with one of the bases of value set out in IVS 104 Bases of Value. (IVS page 5)

Valuer

A “*valuer*” is an individual, group of individuals or a firm who possesses the necessary qualifications, ability and experience to execute a valuation in an objective, unbiased and competent manner. In some jurisdictions, licensing is required before one can act as a valuer. (IVS page 5)

Value at Risk

The maximum loss that could be expected to be incurred over a nominated time period as a result of movements in identified risk parameters, within a specified level of probability based on statistical analysis of historical price trends and volatilities.

See also: Business Risk; Financial Risk; Market Risk; Systematic Risk; Systemic Risk; Unsystematic Risk

Value in Use

IFRS Definition from IAS 36: “The present value of the future cash flows expected to be derived from an asset or cash-generating unit.”

W

Weight

The word “*weight*” refers to the amount of reliance placed on a particular indication of value in reaching a conclusion of value (eg, when a single method is used, it is afforded 100% weight). (IVS page 5)

Weighting

The word “*weighting*” refers to the process of analysing and reconciling differing indications of values, typically from different methods and/or approaches. This process does not include the averaging of valuations, which is not acceptable. (IVS page 5)

Wasting Assets

Assets which in real terms will generally depreciate in value over time.

Weighted Average Cost of Capital

A discount rate estimated by the weighted average, at market values, of the cost of all financing sources in a business enterprise's capital structure.

Working Capital

The amount by which current assets exceed current liabilities. See also: Current Assets, Current Liabilities

Y

Yield

The return on an investment. Usually expressed annually as a percentage based on an investment's cost, its current market value or its face (par) value. Often used with a qualifying word or phrase. See also: All Risks Yield; Initial Yield; Reversionary Yield; Yield to Maturity

Yield to Maturity

The annual rate of return anticipated on a bond if it is held until the maturity date taking into account the current market price, the par value, coupon interest rate and the time to maturity. See also: All Risks Yield; Initial Yield; Reversionary Yield; Yield

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