

# Identification of Methodology Used in Real Estate Property Valuation

Tanuj Parmar<sup>1</sup>, Hiren Mori<sup>2</sup>, Dhanesh Poriya<sup>3</sup>, Vaibhav Vanani<sup>4</sup>, Sandip Chauhan<sup>5</sup>,

Yash Bhagat<sup>6</sup>

<sup>1</sup>Assistant Professor, Dept. of Civil Engineering, Government Engineering College, Surat(GJ), India.  
<sup>2,3,4,5,6</sup> B.E. Student, Government Engineering College, Surat, Gujarat, India.

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**Abstract** - Valuation is the technique of determining the value of a property such as commercial, residential agricultural land and industrial. value is determined on basis of its selling price and rent or income it can fetch. The purpose of this paper is to introduce people with general field practice of valuation of real estate property. This study is based on systematic research in the field of valuation. It will be helpful to all the users as well as professionals who want to work as a value. This study covers the methodology verified by the government approved valuer and concerned field expert. The finding of this paper is likely to have important implications in the valuation profession. This study directly introduces users with actual practice of valuation carried out in the field so that they can compare the theories and actual methodology. This study will result in stimulating debate and a realization of a need for a theory which supports a validated process of valuation.

**Key Words:** Methodology, Real estate property, Field practice, Valuer, Valuation.

## 1. INTRODUCTION

Valuation is the process of determining the value of properties such as residential, commercial and agricultural land. Motivation for this study emerged from the examination of general survey of students about their knowledge about field practice of valuation. This study contains details about valuation practice and basic knowledge about actual work methodology. Valuation of firms and projects is the core topic in business and finance. Valuation is carried out basically for financial activities in the economy i.e. Investment, buying and selling, loan and mortgage etc. Generally real estate covers residential, commercial and vacant land.

## 2. OBJECTIVES

Prime goal of this study is to identify the methodology of valuation work for the complete understanding of field practice. Purpose of this study is to identify the differences in actual valuation practice and exact methods.

## 3. SCOPE

This study contains details about field practice of valuation so that students come to know hours of discussion on valuation with valuer. Students can study this information and can research for further improvements required in

execution and its interpretation as well. This study contains information about what are the factors affecting valuation and its extent. Exact methodology is explained by the experienced valuer so there will be more beneficiary to all users for study.

## 4. PURPOSE OF VALUATION

- Buying or selling property:

Valuation done by both party before buying or selling property. Valuation plays key role in real estate market transactions.

- Assessment of tax:

Valuation determines the actual value of property for tax purpose and it considers the comparable home sales in recent time.

- Determination of Rent:

Valuation is must for the fair rent fixation of the property. Especially when property is rented by the government or semi government organization.

- Mortgage and security of loans:

While advancing any sum of money on the mortgage or security against property, the mortgager and bank both carry out value of property and then take decision for the lending of money.

- Insurance of property:

People are now becoming more concerned about their security for the property and they take help from valuers for insurance valuation.

- Betterment charges:

Betterment fee would be levied on property which got benefit of price rise due to any infrastructural development like metro, industrial corridor, expressway etc. due to better connectivity and facilities betterment charges is determined by the proper valuation.

- Merger and Takeover:

Valuation of assets is carried out in merger and takeover it involves modeling future cash flow associated with an investment and then deciding how to value those cash flows.

- Other purposes:

Stamp duty, Dissolution of partnership, advance payment against work in contract, bank guarantee, revaluation, auction, property transfer, Foreign collaboration, import duty, visa, family partition, divorce and housing loan etc.

### 5. LITERATURE REVIEW:

- Rent capitalization method / Income capitalization method:

In this method valuation is calculated as per net income that property may fetch. Value of the property is calculated by Net income multiplied by year's purchase. When record of rent is available this method is suitable.

Value is determined by capitalizing the net yearly Rental Income at a prevailing rate of Interest and rate of Capitalization.net income worked out by deducting outgoings like municipal tax, repairs, support benefit charges, Insurance premiums, rent collection and management charges etc.

- Based on profit method:

This method is used to carry out valuation of Hotels, Cinemas, and Marriage Halls. The name suggests it deals in working the profit from the property subsequently capitalizing it.in this method capitalized value depends on profitability of business not only on land and building itself.

- Depreciation method:

This method is suitable for buildings when detailed measurements are available and accurate valuation is required deducting depreciation of each component.

- Development method:

This technique is utilized to assess such property where there is a formative potential, with the goal that estimation of property after improvement will be expanded more than the use brought about, for instance vast part of land can be partitioned in little plots and grew completely to give plots of land to private social orders, or a substantial complex of multistoried structures, shopping/business complex and so on. In such case the cost is chosen per section of land. The cost can be landed at by evaluating the cut plot rates in the region balanced by the accompanying certainties:

- Cost of Development (20%) : It incorporates
  - Roads ,Gardens/Parks, Underground drainage, Electric mains and sub station Earth filling/cutting, Municipal charges, Sewage
- Professional Charges to Architect, Engineer

- Cost of acquiring Vacant Possession from the current inhabitant is required.
- Developers Profit: 15-25%

This method suitable when valuation required for undeveloped or partly undeveloped and developed property. In this method valuation is carried out by deduction of road and park area from large area of plot.

- Direct comparison approach method/ Sales comparison method:

In this method valuation is carried out by the comparison with similar properties nearby in this method first identify the similar property then analyze the sale prices and determine the value of the certain property. It is suitable when rental value is not available but evidence of sale price of similar property is available.

- Valuation based on cost / Cost Approach / Land & Building method:

When cost incurred in constructing building or in possessing of building is taken as basis for valuation this method is suitable .In this method the present value of land and building calculated separately and summation of this is final value of the property.

### 6. METHODOLOGY

Valuation is carried out by many methods depend upon circumstances and type of property. Availability of data also plays vital role in choice of method for certain type of property. Methodology is shown in figure.

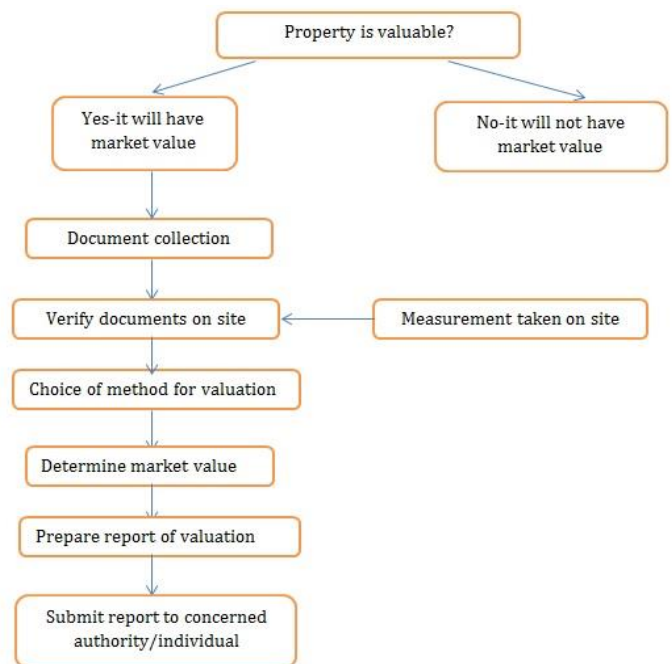


Fig-1: Methodology used in valuation

## 7. SYSEEM OF GENERAL VALUATION PRACTICE FOR RESIDENTIAL PROPERTY:

As per study of collected documents from valuation firms and discussion with valuers, identification of system of general valuation practice for residential property is done which is described below.

- Document Collection:
  - Approved plan / site plan and detailed construction drawings (architectural, structural and foundation details, sections) as per actual construction done along with layout plan for various services i.e. water supply, sanitary, fire protection system layout
  - Actual date of start and completion of construction with documentary evidence.
  - Account details of property for information of development charge and other incurred expenses on property
  - Copy of lease deed/sale deed of land for property.
  - Share in property of client.
  - N.A. certificate
  - Possession letter
- Scrutiny of documents by site inspection and measurements from client/bank/user.
- Choice of appropriate method as per suitability given above.
- Market survey for current selling price of similar property with similar circumstances.
- Data interpretation.
- Determination of final value as per method of respective valuation method.
- Report preparation for respective value of property.
- Report submission to client/bank/user.

## 8. PROCEDURE INVOLVED IN ACTUAL FIELD:

### 8.1 Land and building method / Cost approach:

In this method the present value of land and building calculated separately and summation of this is final value of the property.

#### ❖ PROCEDURE INVOLVED

- Identify the exact purpose of applicant for what valuation is supposed to be carried out
- Collect necessary documents and verify the measurements and its extent on site
- Take suitable unit rate based on prevailing market rate of recent comparable property nearby.

- Calculate value of building as per current construction cost per unit area and apply depreciation as per condition of property.
- Determine the land value by the market survey of recent rate of land nearby.
- Apply modifications according to the purpose of valuation.
- Prepare Report of valuation
- Submit report to concerned authority or individual.

### 8.2 Rent capitalization method / income capitalization method:

In this method valuation is calculated as per net income that property may fetch. value of the property is calculated by Net income multiplied by year's purchase.

#### ❖ PROCEDURE INVOLVED

- Identify the exact purpose of applicant for what valuation is supposed to be carried out
- Collect necessary documents and verify the measurements and its extent on site
- Calculate net income by substituting outgoings and if rent is not revised by owner then take rent as per prevailing market rent.
- Value of the property = Net annual income x year's purchase
- Apply modifications according to the purpose of valuation.
- Prepare Report of valuation
- Submit report to concerned authority or individual.

### 8.3 Sales comparison method / Direct comparison approach:

In this method valuation is carried out by the comparison with similar properties nearby in this method first identify the similar property then analyze the sale prices and determine the value of the certain property.

#### ❖ PROCEDURE INVOLVED

- Identify the exact purpose of applicant for what valuation is supposed to be carried out
- Collect necessary documents and verify the measurements and its extent on site
- Identify the similar property.
- Analyze the sale prices.
- Establish the value by the comparison with similar properties that have been sold.
- Prepare Report of valuation
- Submit report to concerned authority or individual.

## 9. CONCLUSION:

This research work results into identification of procedure involved for the valuation of properties. In this study brief explanation of methods used for valuation is described. This study explains whole procedure in simple steps so that users can easily understand the methodology of actual work carried out for the valuation of property. This study is the foundation stone for the further research work and detailed analysis of every aspect of this field practice. Procedure which is described in this study is general method which is used by most of the valuers. Work order for valuation is standardized based on these three method of valuation. Outcome of this study is that every work is designed and executed as per valuer's personal opinion and experience so same work may be done by different tasks. Lack of Standardization in execution of work is observed in this study. Procedure described in this study is sufficient for the complete understanding of valuation work.

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