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**Sent:** Wednesday, 3 October 2012 1:39 PM
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**Subject:** Valuer Alert - Valuing New Product - Guidance to API Members

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# Valuer Alert - Valuing New Product - Guidance to API Members

## Welcome Mark Ruttner

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**VALUING NEW PRODUCT – GUIDANCE TO API MEMBERS**

There continues to be debate in the property community regarding valuations of new residential developments. The main concerns raised suggest inconsistency in valuation approaches/advice, including the basis on which the valuation is made.

Where a valuer is instructed to determine the market value of a property for first mortgage security purposes the following well established definition applies.

The International Valuation Standards Council International Valuation Glossary defines **market value** as:

"The estimated amount for which an asset or liability should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion."

Further clarification is provided in the PropertyPRO Supporting Memorandum regarding determining the market value for a new individual unit or house:

"What the subject property could be expected to sell for if offered as an individual property through a competent local agent adopting a marketing strategy that would normally apply to a property of this nature being marketed as an individual property".

This clause is supported by another extract from PropertyPRO as follows:

"PropertyPRO is specifically designed to assess the market value of a single residential property to be held as security for first mortgage purposes. As such its value must be assessed on the basis upon which it is, or is intended to be, held as a security

In principle, these clauses mean that when determining the market value of a new residential property, the valuer should have regard to the selling practices that would normally apply to an individual owner selling an individual residential property. It is therefore clear that where a valuer is instructed to determine the market value of a new residential unit or house sold using selling practices not normally available to, or applied by an individual owner selling an individual residential property, the valuer must give consideration to whether or not the sale price could be readily achieved by a local agent selling to an informed buyer or whether the selling practices have resulted in a sale price that differs from the definition of market value.

In order to provide the client with a credible valuation report, it is vital that a consistent valuation approach be adopted when it comes to the assessment of the market value of a new individual residential property, or any other property for that matter.

**The following additional comments are provided:**

<u>Dealing with sales in the same development/project.</u>

The valuer should always use the best evidence available. Given the principles / guidance above, the developer sales may not provide the best evidence if the methods used to sell the property are not readily available to an individual owner (e.g. significant market budgets).

With this said, sales from within the development are still considered as are sales from other developments having regard to the marketing strategies that have been applied. Once the valuer has reviewed the evidence, it may be determined that property transacting in the same development/ project is transacting at market value despite the marketing strategies adopted by the seller.

Once a development is complete and the initial developers marketing campaign is finished, the property will be in competition with any comparable new completed units on the market. If the new residential property was offered for resale, the valuer should consider if any strategies, incentives or inducements offered as part of the original marketing campaign are available to be passed on to a new purchaser. Where this is not possible, and the evidence from other developments suggest that the prices paid in the complex have been distorted as a result (i.e. sold above market value), it is appropriate that the valuer assesses the property based on the long standing definition of market value, which would exclude the value of the inducements.

Re-sales in a complex can provide good evidence of value (provided they are researched to ensure they are not buy-backs).

Valuers should always include sufficient comparable sales that are not developer sales or sales in the same "new" complex/estate to establish the market value of the individual unit/house.

<u>Are you valuing new or second hand product?</u>

The property is new and should be valued as new. The guidance is around the "premium for new".

After adjusting the valuation for the impact of any selling practices, it is still likely that the market will apply a "premium for the new product" over the prices paid for similar older stock. A broad analysis of the evidence is required to determine the amount.

Provision of information on "inducements".

Developers and or their representatives are on occasions reluctant to provide details of inducements, however, this should not discourage the valuer from investigating the level of incentives /inducements in the marketplace. The valuer should request details of all inducements from the marketing agent for all properties (including comparable sales – to allow for correct analysis). If this information is refused by the agent, the valuer should make appropriate comments in the report that inform the lender of the concerns.

Whilst this knowledge allows for better analysis of sales, it does not necessarily follow that the sale price less the dollar amount of the incentive equates to market value.

The International Valuation Standards Council publication IVS 2011 includes the document - IVS 310 Valuations of Real Property Interests for Secured Lending. The following is an extract from that document:

"It is not uncommon for a seller of property, especially a property developer or trader, to offer incentives to buyers. Examples of such incentives include rental income guarantees, contributions to the buyer's removal or fitting out costs, or the supply of furnishings or equipment. Market value ignores any price inflated by special considerations or concessions. Where such exist, it is appropriate to comment on the effect that any incentives being offered have on the actual selling prices achieved as the incentives may not be available to the lender in the event that it had to rely on the security."

A reduction in the contract amount for non-standard marketing costs or other inducements should not be automatic. The valuation should have primary regard to comparable evidence that did not include any such non-standard marketing costs or inducements. A simple deduction of the marketing costs or inducements may result in a figure that departs from the principles of market value.

Not all incentives or inducements will have the same impact on market value. For example, inducements such as fencing, driveways, landscaping etc. may "add value" to the property, particularly if the valuer is instructed to determine the market value "as if complete". Other inducements, such as furniture packages (that can be removed), free vehicles and straight "cash back" incentives etc are unlikely to be available to a lender in possession or to a buyer if the property was to be resold. The valuer should consider the impact on value and make the appropriate adjustments for these items and provide relevant comments to explain their rationale.

Sustainability requirements in building new product.

New building requirements for the inclusion of energy efficient fittings or water saving measures should be acknowledged. Comparable sales of properties with similar inclusions should be used where available as the primary evidence so that any difference between older properties completed prior to the current requirements and newer properties that comply with the current requirements can be identified. This reinforces the comparison of "like with like" which is the primary consideration in all valuations.

The valuer has to deal with market value, which does not necessarily equate to cost. Like innovative design aspects etc, valuers have to make a judgement call on the impact of additional items until evidence is available that substantiates the impact on value.

Communication

The valuation report needs to articulate a valuers reasoning for adopting a certain position on the value assessed. This is particularly so if the valuation does not support the purchase price so that all affected parties can understand the basis on which a valuation for mortgage