

Real Estate Valuation for Special Purposes in Poland

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Key words: valuation, market value, limited property market

SUMMARY

The issue of real estate valuation in Poland is regulated by Acts of Parliament and Regulations of the Council of Ministers. They define the approaches, methods and techniques of valuation and indicate the conditions and limitations of their application.

The Polish Federation of Valuers Association has developed a set of professional standards which are binding for real estate valuers. However, in practice, valuers find it difficult to establish the market value of, e.g.:

- the real estate which will be developed, improved or money will be invested into it,
- the real estate with buildings on it which are to be pulled down,
- the real estate situated in an area where no such plots of land have been sold to date,
- land which, in the local area development plan, is intended for urban greenery,
- land whose right of perpetual usufruct has yet to be valued,
- land under roads,
- real estate remaining outside the borders of Poland.

These are examples of valuation where the market for such real estates is limited or non-existent, and consequently, there are no sale prices for similar real estates.

STRESZCZENIE

Nabywanie nieruchomości przez cudzoziemców w Polsce wymaga specjalnego zezwolenia wydawanego w drodze decyzji administracyjnej. Po 2004 roku (wstąpienie Polski do Unii Europejskiej) zezwolenia te dotyczą głównie obywateli państw spoza Europejskiego Obszaru Gospodarczego. W stosunku do obywateli Unii Europejskiej obowiązują okresy przejściowe (nieruchomości rolne i leśne oraz tzw. drugie domy). W pracy przedstawiono procedurę nabywania nieruchomości przez cudzoziemców w Polsce.

Dokonano też szczegółowej analizy natężenia tego zjawiska w latach 1990 – 2005, z uwzględnieniem roku 2005. Dane źródłowe uzyskano ze sprawozdania Ministra Spraw Wewnętrznych i Administracji.

Sprzedaż nieruchomości cudzoziemcom nie wywiera istotnego wpływu na rynek nieruchomości w Polsce.

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1. INTRODUCTION

Due to the increasing significance attributed to real estate and its value in the process of taking various economic and political decisions, it has become necessary to develop and propagate knowledge of land management as well as the principles and methods of real estate valuation.

The knowledge of real estate value and the basic factors which affect it are required of government and self-government administration workers.

The links between financial institutions, insurance companies and developers, on the one hand, and real estate owners on the other, are becoming noticeably stronger.

These tendencies have resulted in the emergence of three real estate-related professions in Poland: certified real estate valuers, land manager and real estate agent. The qualifications necessary for these professions have been laid down in the law of real estate management.

Applying the principles of market economics to the decision-making process in land management has prompted a discussion on unifying the opinions in the field as well as determining new areas of research, which would concern, for example, real estate valuation.

The issue of real estate valuation in Poland is regulated by legal and professional standards. The term “real estate valuation” denotes the process of valuing a real estate as the subject of the right of ownership and other rights to the real estate.

Real estates can only be assessed by certified valuers.

A real estate valuer is a person qualified to value real estate. The relevant certificate is issued by the Minister for building construction, pursuant to the provisions of the law of real estate management.

2. TYPES OF REAL ESTATE VALUE AND METHODS OF ITS VALUATION

Provisions of the law of real estate management relate to the valuation of any real estate, regardless of its type, location and intended purpose, ownership and purpose of valuation. The following can be performed in the process of valuation:

- determination of the market value,
- determination of the cost value,
- determination of the cadastral value,
- determination of other types of value, provided for in separate provisions.

A comparison or income approach, together with related methods and techniques of valuation, are applied in real estate valuation. If the existing conditions render the approaches impossible

to apply, the real estate market value is determined by a mixed approach. The reproduction value, in turn, is determined by the cost approach. Real estate valuation methods are classified as shown in Fig. 1 and in Fig. 2. The real estate cadastral value will be determined with the use of methods relevant to mass valuation, applying statistical models and methods.

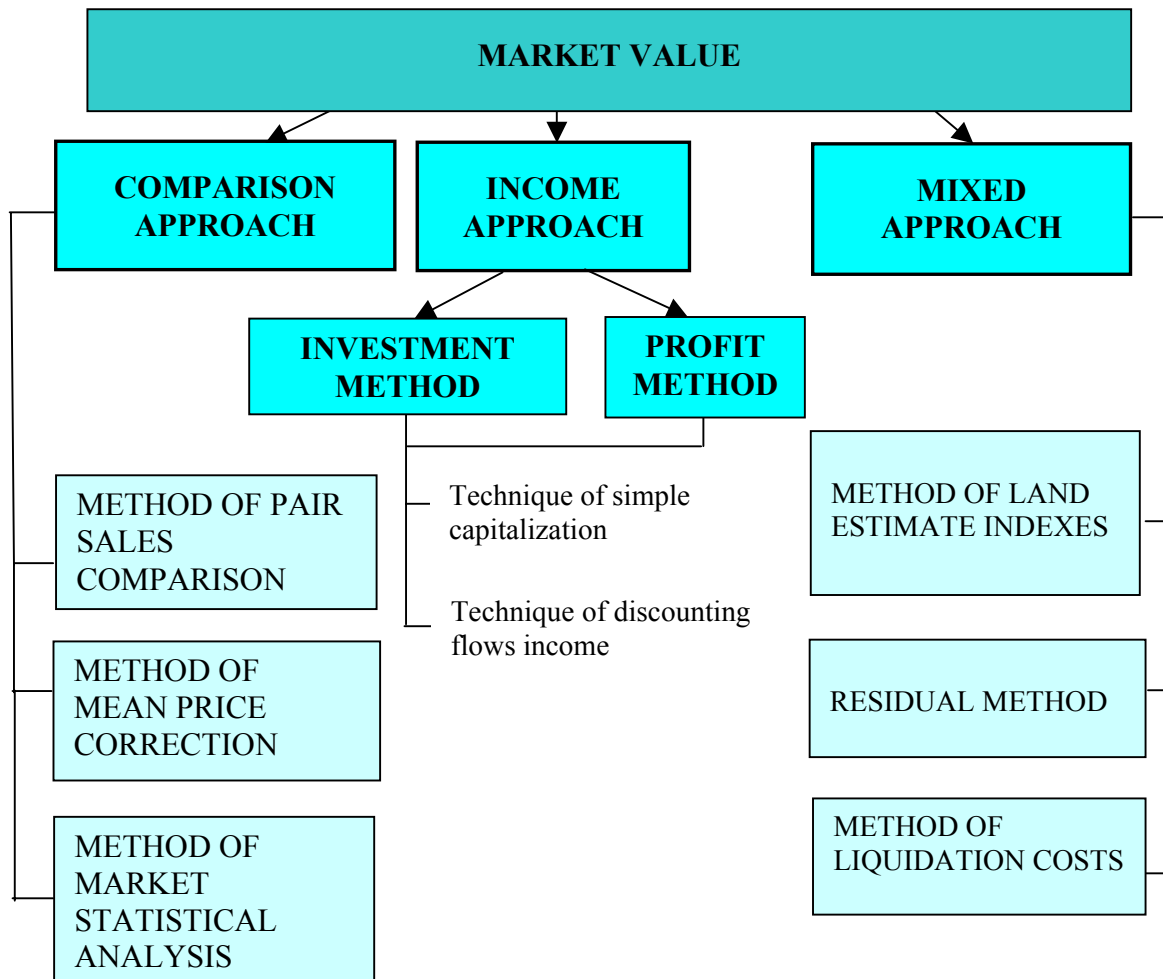


Fig. 1. Classification of methods of market value valuation

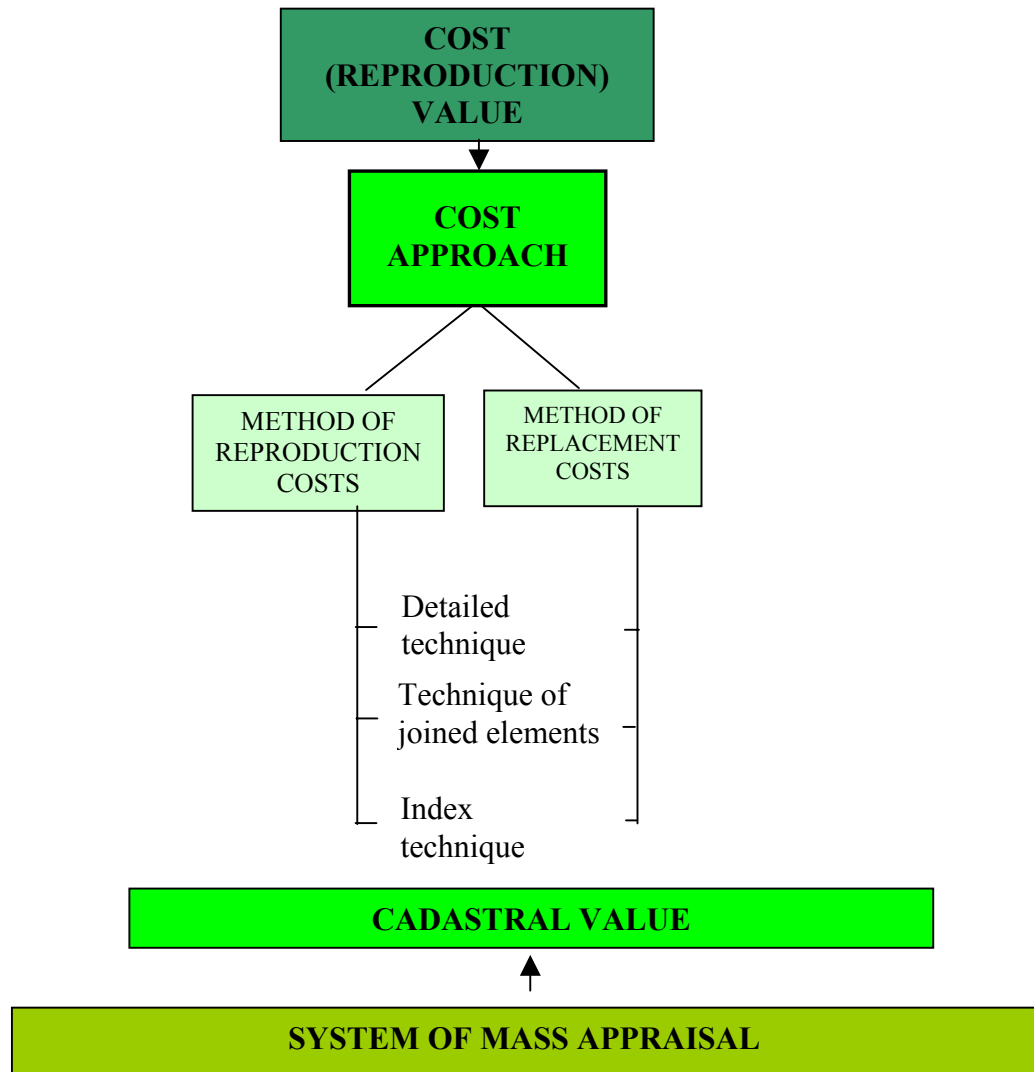


Fig. 2. Classification of methods of non – market value valuation

The appropriate approach, method and technique of real estate valuation are chosen by an valuers. However, the valuers has to take into account the purpose of the valuation, type and location of the real estate, intended purpose of the real estate in the local area management plan, fitting with technical infrastructure, its development and the available data concerning the prices, income and characteristics of similar real estates.

According to the provisions of the law of real estate management, an valuers has the right and obligation to exploit all the necessary and available data concerning the real estate in the process of real estate valuation located in:

- land register,
- land cadaster,
- registers of land technical utilities,
- local land development plans,
- registers kept by tax offices,

- documents held by the agencies, which have been entrusted with exercising the right of ownership by the State Treasury by means of the relevant acts of Parliament.
- Legislators have obligated institutions to make the data contained in the documents in their possession available to real estate valuers.
- It should be emphasised that information about transactions entered into under extraordinary circumstances, which resulted in establishing a price considerably different than the average market price, must not be a source of information about transaction prices. The following are considered to constitute extraordinary circumstances: real estate sales executed in enforcement proceedings, sales with a discount, sales with a postponed payment date or sales with a postponed date of transfer to the purchaser. Prices obtained in the sale by auction can be a source of information concerning transaction prices if they do not deviate from the average market prices by more than 20%.

3. VALUATION OF A REAL ESTATE IN SPECIAL CIRCUMSTANCES

Real estate valuers find it difficult to value a land real estate if there are no similar real estates available in the area. This is the case when an unusual real estate is being traded, of the type that is rarely found on the market.

Several such examples are presented below. They are accompanied with the methods applied by valuers in order to value the real estate or the right related to such a real estate.

3.1. Valuating a real estate which is to be developed

If work is planned on a real estate, aimed at construction, extending or rebuilding of an existing building, the market value of such a real estate is determined by the residue method.

The value is determined as the difference between the value of the real estate after completing the work and the average cost of such work. The investor's profit, earned on the market of similar real estates, should also be taken into account.

The residual method can be applied if the following conditions are met:

- in the circumstances, it is impossible to apply the comparative or income approach to the valuation,
- the type and scope of the construction work is known,
- the elements of the relevant approaches adopted for the method include the data which reproduce the market conditions.

Detailed reasons for applying the residual method of valuation have to be provided in the valuation study.

The market value is determined with the use of the following formula:

$$V_1 = V_2 - (C_D + P)$$

where:

V_1 – the value of a real estate as of the valuation day

V_2 – the value of a real estate after the construction work has been completed

- C_D - the cost of development,
 P - investor's profit,

Valuation of a real estate with development potential or feasibility studies can be performed for various purposes. The most important of them are the following:

- determination of the maximum purchase price for a plot of land with a view to erecting a building or rebuilding existing ones, assuming an acceptable profit margin and assessed development cost.
- determination of a probable profit level which can be earned by improving a real estate if the cost of a plot of land and the cost of its improvement are known.
- determination of the maximum costs of a real estate development, taking into account the minimum acceptable level of profit and the known price of the real estate in its current condition.

Due to the fact that many factors related to both the expected income and the assumed cost of development as well as to the expected cost of development and the risk related to investment are determined with a wide error margin, the results should be treated with caution.

3.2. Valuation of a real estate built up with objects to be demolished

If the real estate components are to be liquidated, the method of liquidation costs is applied. Application of this method to real estate valuation requires that detailed reasons should be provided in the valuation study.

The real estate value, determined by the method of liquidation costs, equals the cost of land acquisition less the cost of liquidation of its components.

The cost of liquidation of components of a real estate is determined by the techniques typical to the cost approach. The real estate value thus determined is increased by the value of materials remaining after liquidation of the real estate components.

According to the provisions, the market value of a real estate determined by the method of liquidation costs is calculated from the following formula:

$$V = C_A - C_L + V_M$$

where:

- V - market value of the real estate as of the valuation day,
 C_A - the cost of land acquisition (market value of un-built parcel),
 C_L - cost of liquidation of land components,
 V_M - the value of the recyclable materials.

The cost of land acquisition is adopted as the market value of land with the same characteristics. The cost of land acquisition is the cost of purchasing land with the same function (use) and utility features and as similar as possible to the appraised land, taking into account its location.

Determining the cost of liquidation of land components and the value of recyclable post-demolition materials are determined instead of the reproduction cost, also taking into account the cost of demolition or liquidation.

If there is no possibility of recycling the rubble, the calculation of the real estate value should include (in minus) the cost of storing rubble at the dumping site.

3.3. Determination of the market value of agricultural land

The method of land value estimation indexes is applied in the valuation of agricultural land if there are no similar transactions.

In this situation, the land value is estimated as the product of the estimation index for 1 ha of the land and the price of 1 quintal of rye grain. The price of rye applied at the local market is taken in the calculation.

Soil productivity are adopted according to the data from the real estate cadaster. The land revenue district is adopted according to the regulations concerning the agricultural tax.

The estimation indexes are established officially, depending on soil quality. Table 1 presents a fragment of such a list. According to this method, the value of agricultural land is calculated according to the following formula:

$$V_{AL} = \sum_{i=1}^n I_{ij} \cdot P \cdot S_i$$

where:

V_{AL} - market value of agricultural land,

I_{ij} - an estimation index in quintals of rye from 1 ha of arable land situated in the j-th land revenue district,

P - the price of 1 quintal of rye,

S_i - the area to which the estimation index refers.

Table 1 Estimation indexes for arable land, grassland and permanent meadows:

a) for arable land

Tax district	Estimation indexes in quintals of rye grain per 1 ha of arable land				
	classes of land				
	I	II	IIIa	IVb	VIz
I	145	132	118	60	8
II	126	115	103	52	5
III	110	100	90	46	1
IV	94	85	76	38	1

b) for permanent meadows and pastures:

Tax district	Estimation indexes in quintals of rye grain per 1 ha of meadows and pastures		
	classes of land		
	I	II	VIz

I	145	118	5
II	125	103	3
III	110	90	1
IV	94	76	1

Source: Journal of Laws of 2004, No. 207, item 2109

3.4. Valuation of real estate overgrown with trees, bushes or forests

If there are no relevant transactions, the following situations are considered:

1) the land is situated in an urban investment zone and is publicly accessible. These include parks, ornamental gardens, green areas or protective zones of forest.

The value of the real estate is the sum of the value of the land and the value of bushes, trees and other plants on the land; the following factors are also taken into account:

- it is assumed that the value of 1 m² of the land equals 50% of the value of 1 m² of land with the same intended use as that of the majority of adjacent land;
- valuation of the trees, bushes and other plants is based on the cost of planting them and nurturing them until the date of valuation.

2) Valuation of land situated outside zones of urban investment is based on the method of land estimation indexes. The method is described above, under 3.3.

3.5. Market value estimation for a real estate which is the subject of perpetual usufruct right

The following situations should be considered:

- 1) there are transactions (sale and purchase) concerning the right of usufruct of plots of land
 - valuation is performed according to the comparative approach,
- 2) there are no transactions concerning the right of perpetual usufruct of real estate, but sale was executed of the real estate as the subject of the right of ownership,
 - the real estate is valued based on the interrelations between the prices of the rights of perpetual usufruct of real estates and the prices of the right of ownership of such real estates, applied on other comparable real estate markets.
- 3) No transactions concerning the right of perpetual usufruct of a real estate either on the local or neighbouring markets. There is a market for the right of ownership of real estate.
 - a real estate is assessed by calculating the product of the value of the right of ownership of a land real estate without buildings and the corrective coefficient, calculated from the formula:

$$C_C = \left(1 - \frac{r}{R}\right) \cdot \frac{t}{T} + 0,25 \cdot \frac{T-t}{T}$$

where:

C_C - the corrective coefficient;

r - annual payment rate, not higher than 3%;

t - the number of years when the right of perpetual usufruct was not exercised;

- T - the number of years for which the right of perpetual usufruct was established
 R - the average capitalisation rate, based on examination of real estate market by an valuers; the capitalisation rate ranges from 0,9 to 0.12.

So:

$$V_{pu} = V_o \cdot C_C$$

where:

- V_{pu} - value of perpetual usufruct of real estate
 V_o - value of the right of ownership

The formula can be applied to estimate the value of the right of ownership if the market exists for the right of perpetual usufruct right. The value of the right of ownership can be expressed by the following formula:

$$V_o = V_{pu} \cdot \frac{1}{C_C}$$

3.6. Valuation of land under roads

As a matter of principle, transaction prices for land under roads are applied in valuation.

Difficulties in valuation arise when no data concerning the prices of similar land exist. The following rules are then applied:

- 1) the value of a plot of land allotted for public roads or broadening of existing roads is calculated as the product of the value of 1 m² of the land from which the plots of land were sectioned off and their area. If the plots of land were sectioned off from agricultural or forest real estates, their value is increased by 50%;
- 2) the value of land already occupied by roads is determined as the product of the value of 1 m² of land with the same intended use as the majority of adjacent land and its area.

If the majority of adjacent land is used as agricultural land or forest, their value is increased by 50%.

These principles are applied for establishing compensation for the plots of land expropriated for motorway construction.

3.7. Valuation of land acquired with a view to improving the conditions of building construction on an adjacent plot

A real estate or its part, which is to be sold to the owner of an adjacent plot of land cannot be valued directly, based on the analysis of the real estate market. Such real estates are not subject to free trade on the market. Due to their size (or sometimes shape) they cannot be regarded as building plots. Such a plot of land can be purchased only by the owner of an adjacent plot, who purchases it with a view to improving the quality of their real estate.

The value of such a real estate is determined as the difference between the value of the adjacent real estate together with the real estate or its part which is to be purchased, and the value of the adjacent real estate before the purchase of the real estate or its part.

The value of buildings of the adjacent real estate are not taken into account in determination of the difference.

3.8. Valuation of real estate left behind outside the borders of Poland

Real estate outside the borders of Poland is assessed if its value is to be recognised against the price of a real estate purchased from the State.

It is a kind of compensation for people who lost their property in connection with World War II.

Such real estates are assessed based on data from similar real estate markets in Poland, in the provinces and cities which are comparable in terms of the degree of urbanisation and the population to those where the real estate was left.

The following provinces are regarded as comparable; coefficient correcting the differences in the level of economic development are also provided (example):

- Province of Lviv – Podkarpackie province, coefficient - 1.0;
- Province of Vilnius – Podlaskie province, coefficient - 0.64;
- the city of Lviv – the city of Kraków, coefficient - 1.0;
- the city of Vilnius – the city of Lublin, coefficient - 1.0.

Real estate in those locations is assessed based on the prices in those provinces or cities for similar real estates.

4. SUMMARY

The paper presents examples of the valuation of real estates on restricted markets, applied by valuers in Poland. The methods are in conformity with the law. However, they do not solve all the problems which may arise in real estate valuation. It is still not easy to assess plots of land in city centres. All the land is built up, so there are no non-built-up plots of land for sale. It is also difficult to find similar neighbouring markets as most city centres are built up.

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BIOGRAPHICAL NOTES

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Academic experience: Land Surveyor and Land Management MSc, University of Warmia and Mazury in Olsztyn, Professor in the field of technical sciences

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Practical experience: licensed valuer, coordinator of many projects connected with property development, creation of land value maps, land information systems

Activities in home and international relations:

President of the Polish Real Estate Scientific Society

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Member, Editorial Board International Journal of Strategic Property Management, 1989 –

Member, Polish Surveying Society, 1975 –

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Hong Kong SAR, China, 13-17 May 2007

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