

Market Rent vs. Contract Rent in Connecticut Assessment and Valuation Practice

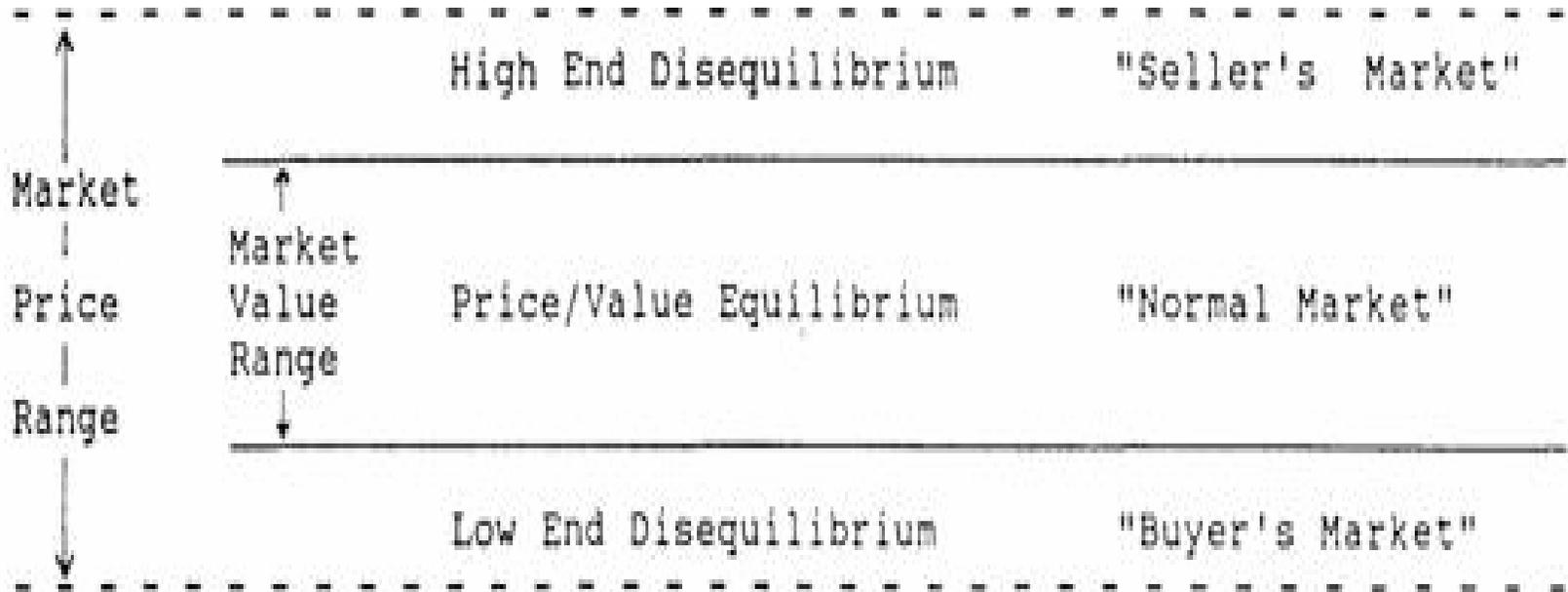
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Starting Where We Left Off

(Last Two Slides from Assessor's School on June 6th)

Price/Value Relationship Revisited



Starting Where We Left Off (continued)

- Not every price is an indicator of market value.
- Beware of and take a hard look at the outliers when analyzing your market.
- The high-end or low-end land sale may not reflect the actions of the typical purchaser.
- The same goes for the high-end or low-end property sale.
- Appraisal Basics: One sale does not make a market.

Definitions of Market Value

Market value is defined in the appraisal rules of the Federal Financial Institution Regulatory Agencies as:

The most probable price a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably and assuming the price is not affected by undue stimulus.

Definitions of Market Value (cont'd)

Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

- **Buyer and seller are typically motivated.**
- **Both parties are well informed or well advised and are acting in what they consider their best interests.**
- **A reasonable time is allowed for exposure in the open market.**
- **Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto.**
- **The price represents the normal consideration for the property sold, unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.**

Definitions of Market Value (cont'd)

Market value is defined in *The Appraisal of Real Estate* (American Institute of Real Estate Appraisers, 13th Edition, 2008, Page 23) as:

The most probable price, as of a specified date, in cash, or in terms equivalent to cash, or in other precisely revealed terms, for which the specified property rights should sell after reasonable exposure in a competitive market under all conditions requisite to fair sale, with the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under undue duress.

Definitions of Market Value (cont'd)

The previous definition of market value is an extension of the term *fair market value* as referenced in early appraisal literature and as still referenced in some statutes.

The Dictionary of Real Estate Appraisal (Second Edition, 1989, Page 113) stated under the term *fair market value*:
See market value.

Definitions of Market Value (cont'd)

The previous definition of market value is also consistent with the accounting term *fair value*.

The Financial Accounting Standards Board in Statement of Financial Accounting Standards No. 157 (September 2006, effective for fiscal years beginning after November 15, 2007) 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.

Definitions of Market Value (cont'd)

NOTE: USPAP Has No Specific Market Value Definition

Market Value: a type of value, stated as an opinion, that presumes the transfer of a property...as of a certain date, under specific conditions set forth in the definition of the term identified by the appraiser as applicable in an appraisal....(comment omitted)...

Appraisers are cautioned to identify the exact definition of market value, and its authority, applicable in each appraisal completed for the purpose of market value.

Market Value of What

Fee Simple Interest:

Absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power, and escheat.

(The Appraisal of Real Estate, 13th Edition, 2008, Page 114)

Market Value of What (continued)

Leased Fee Interest:

The ownership interest held by the lessor, which includes the right to the contract rent specified in the lease plus the reversionary right when the lease expires.

(The Appraisal of Real Estate, 13th Edition, 2008, Page 114)

Market Value of What (continued)

Leasehold Interest:

The right held by the lessee to use and occupy real estate for a stated term and under the conditions specified in the lease.

(The Appraisal of Real Estate, 13th Edition, 2008, Page 114)

Market Value of What (continued)

In Connecticut Assessment Practice, the valuer must *consider* both market rent and contract rent.

First Bethel Associates v. Town of Bethel: The wisdom of Solomon is imbedded in law!

Market Value of What (continued)

In practical terms:

Market Value of the fee simple interest
= market value at market rent.

Market Value of the leased fee interest
= market value at contract rent.

Market Value of What (continued)

An alternate expression:

LCV will provide the client with an opinion of the market value of the fee simple interest in the real estate, considering both market rent and any contract rent, according to the attached appraisal scope of work.

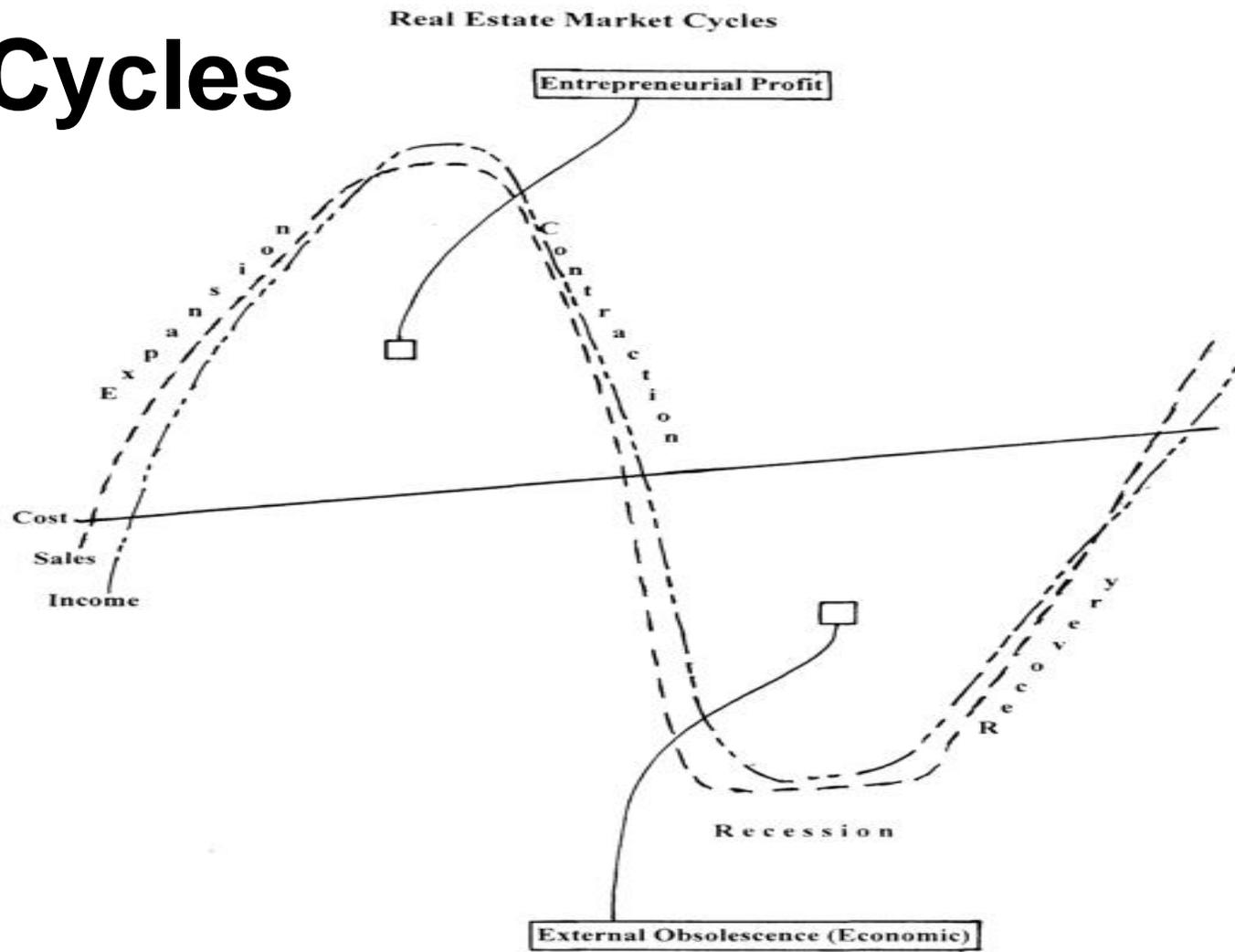
The Big But: Market Rent is based on Contract Rent

How do valuers estimate market rent?

They present and analyze recent contract rents that are considered comparable to the subject space.

Market rent starts out equal to contract rent...but things can change.

Real Estate Market Cycles



So What is a Valuer to Do?

Process a value opinion based on market rent.

Process a value opinion based on contract rent.

Consider the difference, if any, and reconcile the opinions.

So What is a Valuer to Do? (continued)

Process a value opinion based on one or both of the other approaches and consider what light they shed on the situation.

Consider and reconcile: What we are trained to do and have always been doing.

Questions and Comments?

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