When will the Income Approach be implemented in Saskatchewan?

The Income Approach will be used for the 2009 revaluation. The time until then is needed for:

- legislative changes;
- readying computer systems to store, analyze and determine values using this approach;
- conducting research; and
- changing the formulas, rules and principles contained in the *Saskatchewan Assessment Manual*.

In addition, the assessment jurisdictions:

- are organizing and carrying out research;
- are building a new computer system; and
- are beginning data collection in 2003.

Overall Capitalization Rate

For further information please contact

Saskatchewan Assessment Management Agency

Revaluation Unit
306-924-6626 or 866-828-2133
www.sama.sk.ca

or

City of Regina
306-777-7240
www.regina.ca

City of Saskatoon
306-975-3227
www.saskatoon.ca

City of Prince Albert
306-953-4320
www.citypa.com

City of Swift Current
306-778-2777

City of North Battleford
306-445-1781

Saskatchewan Assessment Management Agency

The Income Approach To Value

A New Method of Commercial Property Assessment for Saskatchewan

Market Value = Net Operating Income ÷ Overall Cap

What is the Income Approach?

There are three internationally accepted methods of measuring the value of property: the Cost Approach, the Sales Comparison Approach and the Income Approach. Depending on the nature of the property being valued, one or more of the approaches may be used by the assessment appraiser.

The Income Approach is based on the assumption that the value of a property is directly related to the income it will generate over its economic lifetime. (Property is defined by *The Assessment Management Agency Act* to mean land, buildings and improvements.)

Who will the Income Approach apply to in Saskatchewan?

The Income Approach will initially be applied to:

- apartment/multi-residential;
- hotel/motel;
- office building;
- shopping centre;
- commercial;
- retail; and
- warehouse property owners.

This methodology may not be practical in communities where information on income producing properties is not available. Sound professional appraisal practice requires that an appraiser consider all valuation methods to estimate the value of an asset. An appraiser analyzes accuracy and amount of data available in order to choose the appropriate valuation method.

Why use the Income Approach?

It provides the appraiser with an additional property valuation tool. This increases accuracy in property valuation. The Income Approach is well-proven and widely used throughout North America for income producing properties such as commercial, industrial and investment properties.

How does an Assessment Appraiser use the Income Approach?

Property appraisers analyze income and expense data to help determine an income model.

The values used in the Income Approach are estimated from market data gathered through questionnaires, property owner interviews, published sources and leases. Income and expense data collected by appraisers includes:

- lease information;
- rentable or gross leaseable area;
- number and type of rental units;
- contract rents;
- vacancy rates;
- collection losses;
- miscellaneous income;
- allowable expenses;
- tenant inducements; and
- actual property income and expense information for the current financial period.

Contract rent is actual rent – the rent agreed upon by the landlord and tenant. *Market rent* is economic rent – the rental income that a property would most probably command in the open market. Market rent is an estimate derived from the analysis of contract rents paid and asked on comparable space as of the valuation day.

Only income and operating expenses related to the operation of the property are used for the Income Approach. Expenses are normalized so that the net operating income can be calculated. Various categories of allowable expenses are used in this calculation.

Income or expenses associated with the operation of a business conducted on the property are *not* relevant or used in the valuation of the property.

What about confidentiality?

The assessment jurisdiction recognizes information required may be personal, confidential or sensitive. Steps have been taken to ensure information is kept secure and confidential in accordance with confidentiality provisions in legislation.

What are the basic steps in the Income Approach to Value?

1. Determine the property's *potential gross income* – the income the property would earn at full occupancy and current market rents.
2. Determine the property's *effective gross income* – the potential gross income, minus an allowance for typical vacancy and collection losses, plus any miscellaneous income the property may earn (e.g. parking, laundry and concession income).
3. Determine the property's *net operating income* – the effective gross income minus the operating expenses necessary for the property to earn its potential gross income.
4. Determine an appropriate *overall capitalization rate* using sales of comparable properties with similar physical and locational characteristics. (The capitalization rate is a conversion factor that is applied to the income stream to convert it into an indication of the market value of the property.)
5. Calculate the property's value using the formula:
   Market Value = Net Operating Income ÷ Overall Capitalization Rate