

Course 102 – Income Approach to Valuation

Course Description

Income Approach to Valuation is designed to provide the students with an understanding and working knowledge of the procedures and techniques required to estimate the market value of vacant or improved properties by utilizing the income approach. The material covers real estate finance and investment, capitalization methods and techniques, analysis of income and expenses, operating income, selection of capitalization rates, and application of the approach.

Body of Knowledge

The IAAO Body of Knowledge (BoK) is a framework for defining the key knowledge, skills, and subskills for the mass appraisal profession.

Income Approach to Valuation contains material corresponding with the following Knowledge Areas:

- BOK 2: Collecting and Maintaining Property Data
- BOK 4: Appraising Property



Course Audience

While we do not require prerequisites, it is strongly recommended that prior to taking this course, students take and pass course 101 – *Fundamentals of Real Property Appraisal*. Course 102 assumes students have greater than a cursory knowledge of real property appraisal.

Instructional Methods & Materials

Income Approach to Valuation Online utilizes instructor videos, narrated PowerPoint presentations, interactive online exercises, and frequent checks of understanding through review questions and quizzes to emphasize the main concepts and procedures taught in the course. Students will have access to the following reference materials:

- e-version of the Course 102 Student Reference Manual
- e-version of *Property Assessment Valuation* textbook (PAV)
- Formulas, equations and glossary

Required Technology

Students must have access to the following:

- A computer with a web camera with microphone
- A calculator
- Current version of Google Chrome, Firefox, or Safari
- Current version of Adobe Flash
- If accessing from a mobile device, it must be a large-screen device (i.e., tablet)



Objectives

Upon completion of Chapter 1, you will be able to:

- Recognize the definition of income-producing property.
- Recognize the difference between market value and investment value and know why these differences are significant in deriving value estimates by the income approach.
- Explain how the appraiser's understanding of anticipation, change, and the other basic appraisal principles aids in the analysis of market data necessary in the application of the income approach.
- Understand the relationship between highest and best use and the income capitalization approach to value.
- Recognize the different investor requirements for income-producing properties.
- Recognize the factors that influence the behavior of investors in real estate.
- Identify and explain the various types of financing available to investors in real estate.
- List the sources of financing for purchasing real estate.
- Identify and be able to explain the following components of capitalization rates: discount rate; recapture rate; and effective tax rate.
- Understand the basic concepts of the income approach model and how supply and demand factors interact in specific markets.
- Understand the income capitalization formulas (IRV, which is $\text{Income} = \text{Rate} \times \text{Value}$ and VIF, which is $\text{Value} = \text{Income} \times \text{the Factor}$) in appraising income-producing properties.

Upon completion of Chapter 2, you will be able to:

- Identify the sources of data the appraiser utilizes in estimating income and expense and explain the importance of the accuracy and relevance of market information.
- Identify and explain the various types of rents associated with income-producing properties.
- Identify and understand leases associated with the rental of income-producing properties.
- Understand and be able to derive rental units of comparison in the application of the income approach to valuation.
- Explain the levels of income, potential gross income (PGI), effective gross income (EGI), net operating income (NOI) and the importance of accurate income and expense analysis.
- Identify the categories of income and expense used in reconstructed operating statements of income-producing properties.
- Develop an accurate reconstructed operating statement for appraisal purposes.



Upon completion of Chapter 3, you will be able to:

- Understand the relationship between property income and property value, as expressed by a capitalization rate.
- Understand the components and the functions of the various types of capitalization rates.
- Recognize the formulas that express the relationship between income and value.
- Understand the uses of the IRV and VIF equations in the valuation of income-producing properties.
- Recognize the definition of overall capitalization rate.
- Recognize the practical methods of developing and overall capitalization rate.
- Demonstrate the need for consistency in deriving and applying rates and factors.
- Develop the overall property yield rate from the band of investment technique and extraction from the yield-change formula.

Upon completion of Chapter 4, you will be able to:

- Understand and identify the definition of direct capitalization.
- Identify the mathematical relationships between income and value used in direct capitalization and explain how they are indicated in sales transactions and other market evidence.
- Understand the derivation and application of gross income multiplier in direct capitalization.
- Identify the common symbols used in the income capitalization approach.
- Recognized the procedures used to process income estimates and convert income to value using direct capitalization.
- Understand and identify the definition of yield capitalization.
- Explain the differences between yield capitalization and direct capitalization.
- Identify and understand the definition of an annuity.
- Identify the income stream patterns used in yield capitalization.
- Understand and identify the definition of an annuity.
- Understand and identify the definition of discounted cash flow (DCF) analysis and the components needed for application in yield capitalization.
- Identify the six basic financial functions and the formulas used to compute each financial factor.
- Understand how the compound interest tables can be used for solving common appraisal problems.
- Explain the difference between an effective interest rate and a nominal interest rate.

Upon completion of Chapter 5, you will be able to:

- Understand and be able to select a proper capitalization residual technique in appraising income-producing properties.
- Find value of income-producing properties using the building residual technique.
- Find value of income-producing properties using the land residual technique.
- Analyze the shape and behavior of the income stream.
- Understand the structure of straight-line capitalization.