

European Valuer



Compensating for airport nuisance – the legal context of calculating loss of value



It is uncontested that the operation of airports causes both positive and negative externalities for owners of real estate located in their vicinity. Airport nuisance, associated

mostly with higher noise levels, is becoming increasingly onerous for homeowners as air transport develops and airports enlarge the volume of operations.

Unsurprisingly, the affected landowners seek redress for various negative effects of this phenomenon, with the use of legal instruments that exist either in general legal provisions (neighbour law, tort law, takings law) or have been specifically enacted to deal with these issues (e.g. laws on the protection of the environment). The legislator must thus choose if a dedicated regime of compensation for negative airport externalities needs to be implemented or if general legal concepts are sufficient to resolve the inevitable conflict between homeowners and airports. In addition, the legislator makes important decisions as to the scope of compensatable loss and the rules or procedures according to which this loss should be compensated. Once this is decided in law, it is the role of the valuer to determine the extent of loss, usually by

providing a valuation which shows whether a loss of value has occurred.

“Once this is decided in law, it is the role of the valuer to determine the extent of loss, usually by providing a valuation which shows whether a loss of value has occurred.”

The matter at hand is not confined to one particular country, but has international ramifications, as most airports are expanding and increasing the number of operations. Poland exemplifies a country where air transport is developing rapidly and there is a significant capacity to grow. According to data published by the Polish Civil Aviation Authority, by 2035 Polish airports will have served roughly three times the number of passengers that were served in 2016, thus progressing from nearly 34 million passengers in 2016, to the predicted 94 million in 2035. Compared to the year 2016, in 2017 the number of served passengers increased by 16%, whereas the number of air operations increased by 12%. The above figures explain why once dormant airports are no longer neutral to neighbours, who are experiencing externalities resulting from airport activities.

Although these externalities do have an important positive aspect (regional development, creation of new jobs, investment in infrastructure, economic development), they also cause negative consequences, mostly in the form of noise that was previously negligible or not at a level that warranted opposition.

From a legal perspective, nuisance

caused by increasingly active or entirely new airports is becoming onerous to neighbouring landowners, particularly those who own residential real estate, as the latter is most sensitive to any negative changes in the surrounding environment.

The problem that naturally arises is a conflict between neighbouring uses of land that cannot in its entirety be solved by spatial planning and neighbour law. This conflict may potentially bring about various negative consequences – the most important of which are loss of value, loss of comfort and restrictions on land use.

In addition, the development of airports may cause changes in the prospective development of surrounding areas. The legislator thus faces the need to resolve this inevitable (but not new) conflict in a manner that takes into account the interests of both landowners and the airport itself, which provides services that qualify as those of public utility.

“Although the task may seem to be a rather simple and routine assignment, it is important to bear in mind the legal context of the valuations that are prepared for the purpose of compensation for potential loss of value.”

Valuers usually encounter the problematic situation when being asked to identify the loss of value attributed to negative externalities caused by airport operations. Although the task may seem to be a rather simple and routine assignment, it is important to bear in mind the legal context of the valuations that are prepared for the purpose of compensation for potential loss of value. Firstly, it must be stated that

... continued on page 2, column 1

To contribute an article or to send a letter to the editor commenting on one, contact

jcroberts54@hotmail.com



... continued from page 1, column 3

although the influence of airport operations on homes and their users is similar all over the world, there is no uniform legal approach taken as to what exactly is to be compensated, i.e. whether compensation should reflect only planning restrictions that are usually introduced in areas surrounding the airport (restricted use areas), or whether it encompasses not only concrete restrictions, but also, or sometimes exclusively, less tangible elements, such as loss of comfort and amenity. If the latter applies, the valuer must consider what time period should be contemplated when analysing whether loss of value has occurred and whether there is a particular moment in time (e.g. opening a new runway) that justifies calculating loss of value. It is problematic whether loss of value claims should be brought by homeowners who acquired their home at a discount due to the vicinity of an operating airport and later claim that they have experienced damage in the form of value impairment simply because homes further away are valued higher.

Secondly, there is no uniformity in various legal systems as to whether showing loss of value is sufficient for claiming compensation, or whether loss of value has to be accompanied by impaired use of land, which may in turn be interpreted strictly (have new use/planning restrictions been introduced?) or functionally (are residents factually limited in the use of their gardens, cannot function outside or leave windows open due to noise?). In addition, various approaches are taken concerning the possibility of compensating for a decreased increase in value (damage as lost profits). This is important in areas where real estate prices are rising and yet the neighbourhood surrounding an airport remains unchanged. The valuer may find that some jurisdictions

do not compensate such losses and that homeowners experiencing significant discomfort (like their counterparts living near an airport in a different location) cannot be compensated because the market in their area is strong and the prices are growing.

“It is interesting to note that although the vicinity of an airport causes similar problems for nearby residents, there is no uniform solution that exists in an international context when it comes to possible compensation of homeowners.”

This above issues clearly demonstrate that valuations prepared for the purpose of compensation connected with airport operations are strongly influenced by the legal framework and the scope and assumptions of such valuations must properly reflect the legally prescribed scope of compensatable loss. This may not be an easy task, since even within one jurisdiction it is sometimes difficult to ascertain whether the law prescribes compensation for economic loss (interference from airport operations causes loss of value + expenses for acoustic insulation), or for non-economic loss (interference causes inconvenience), or for some combination of economic and non-economic loss. Nevertheless it is vital to clearly understand what exactly is being valued, since providing a valuation that does confirm a lower value of homes situated near airports is not in itself proof of a causal link between airport operations and a potential loss of value caused by airport externalities.

It is interesting to note that although the vicinity of an airport causes similar problems for nearby residents, there is no uniform solution that exists in an

international context when it comes to possible compensation of homeowners. Indeed, even within one country with different jurisdictions (U.S.A.) various legal grounds are applied, requiring valuations with different assumptions and leading to different outcomes concerning compensatable loss. In England the legislator explicitly excludes any tortious claims and compensation for loss of value resulting from airport operations and considers civil (but not military) aviation as a protected legacy. In the U.S.A., if specified administrative procedures are followed by airports (the Part 150 program) any potential claims for damages are excluded. Such solutions are not, however, universally adopted and the continuing need of valuers to provide valuations in disputes between airports and homeowners remains. Difficulties in ascertaining market values and their fluctuations may be encountered in less active markets (regional airports located in more rural areas).

Another challenge is for the valuation to reflect only the effects of airport nuisance (causality) but not other factors influencing possible decreases in real estate prices and values. Bearing in mind that in disputes, the court or another competent authority relies heavily on the provided valuation, the valuer should be aware of the particular legal context and the purpose the valuation is required for. Understanding what exactly is being valued and what can be compensated ensures avoiding market speculation, overcompensation, and fraudulent claims, thus leading to a socially acceptable and economically viable outcome. ●

Dr. Magdalena Habdas is a qualified real estate valuer, attorney-at-law and Associate Professor at the Faculty of Law and Administration, University of Silesia, in Katowice.

A sea change is upon the Appraisal Institute of Canada, Peter McClean explains



The need for innovation within the appraisal profession is undeniable. Valuation professionals are constantly being challenged by their clients to be more

efficient, to add greater value and to charge lower fees. This reality is particularly evident

in the residential mortgage financing sector, where appraisals are becoming commoditised and other risk-mitigation methods are emerging that may be **“good enough”** for lenders, given Canada’s historically low risk of mortgage default. The Appraisal Institute of Canada (AIC) Board and staff have spent a great deal of time researching and analysing these changes and working to develop strategies

for appraisers to continue to thrive in this changing environment. Technology is fuelling this change and is one of the key industry disruptors within the financial and real estate sectors.

Competition within the lending industry is also becoming increasingly fierce, as non-federally regulated financial institutions

... continued on page 3, column 1



... continued from page 2, column 3

are poised to improve their market share at the expense of the “big five” banks. Shifting consumer behaviours, particularly from millennials who are entering the real estate market, are changing the expectations of the mortgage process, demanding that it be quicker and easily accessible via a smart device – all at a very competitive rate. Millennials’ loyalty to a traditional bank is not like that of previous generations, allowing new institutions with deep pockets to enter the lending industry. As the mortgage lending industry continues to be lucrative, new risk-mitigation models are being offered to lenders. Some providers have begun offering a “**revolutionary approach to valuations in Canada.**” These firms offer various valuation products – from low-ratio valuation using AVMs to desktop/drive-by appraisals, as well as full appraisals that engage field technicians and, in some cases, “**certified appraisers**” – all at a fraction of the time, at an affordable rate and with a unique indemnity insurance to mitigate property valuation risk. If this model, and others similar to it, are accepted by regulators and the big five banks, the impact on the residential appraisal profession as we know it would be significant, with a ripple effect being felt throughout non-residential appraisal assignments as well.

This market reality was the impetus for AIC to proactively engage its national and provincial leadership in a facilitated workshop this February. The purpose of the discussion was to discuss AIC’s challenges within the evolving market, as well as the potential impact of these

challenges to members and to AIC; and to brainstorm potential solutions for the future sustainability and success of AIC members.

“The Appraisal Institute of Canada (AIC) Board and staff have spent a great deal of time researching and analysing these changes and working to develop strategies for appraisers to continue to thrive in this changing environment.”

Impact of industry disrupters on AIC members

During the workshop discussion, participants agreed that the industry disrupters could:

- have a significant negative impact on **residential appraisers**, especially those who have not diversified and rely only on mortgage financing assignments for their livelihood. The impact on residential appraisers would be a decrease in fees, as well as a decrease in mortgage financing appraisal assignments and other point-in-time residential appraisals
- affect **non-residential appraisers**, but at a slower pace. There may be less demand for point-in-time appraisals and more opportunity to become real estate advisors or consultants by leveraging other professional standards beyond the real property standard
- affect **non-fee members**, especially those who specialise in data gathering within large assessment agencies, who may be at risk of being displaced by technology. However, more opportunity may exist in interpretation and analysing data and positioning them as real estate

consultants/project managers within their organisation

- have an impact on the competencies needed by **AIC candidates**. AIC’s current education and training may need to be enhanced to adequately meet the needs of the market in the future.
- Participants saw the future success of AIC members in diversification of competencies and services. Those who resist diversification will be at risk. They also indicated that the **Canadian Uniform Standards of Professional Appraisal Practice (CUSPAP)** provide flexibility and guidance that provide significant potential for AIC members to diversify. There was overall agreement that members must leverage their valuation expertise to become real estate advisors/specialists, add value through thoughtful analysis of data, embrace technology to become more efficient and effective, and utilise other professional standards to diversify their practice.

Next steps

Over the summer and into the fall, AIC, under the leadership of a Board-Appointed Task Force (with senior representatives from the national and provincial levels), will engage with members across the country in order to formulate a clear path forward for our organisation and for the profession as a whole. We are facing what are perhaps the greatest challenges to our profession in our 81-year existence, but I am confident that we are up to the task. ●

Peter McLean AACI P.App is Immediate Past President of the Appraisal Institute of Canada.

Real estate versus the business valuer – one hat or two?



Back in 1990, after four years of experience as a maintenance mechanical engineer in the construction of mines, I would have never imagined that a decade later I would

have started my journey in financial advice as a business valuer (American Society of Appraisers (ASA), 2000) to continue later as a real estate appraiser (2003) and finally as a machinery and equipment valuer (ASA, 2017).

The education system during the communist era did not offer much in the way of finance and accounting skills for

engineering students, so for me everything started with a book about evaluation of investments and projects, where I got the first concepts of NPV and IRR. While working in a Swiss Government project from 1994-96, I was obliged to learn the basics of accounting.

Joining Deloitte in 1999 offered me the opportunity to a second (on-the-job) education, which still continues and I do not think will ever stop.

The basic education we get at university level follows us throughout our life. We can do many training courses afterwards but all of them assume that the basic knowledge of the topic you are being trained in is already known from the university, i.e. the training

course is not a substitute for the university education. You can cover this gap either by sitting at the student’s desk again, or by studying it yourself. The latter is what I did.

The same valuation approaches are used for all asset categories – the difference is in the way they are applied through valuation methods. However, these valuation methods are not always the joy of valuers, depending on their university education. One does not need to have a specific university degree to become a valuer in one category or another. Nevertheless, some valuation methods are more suited to a certain university degree.

If a valuation engagement in real estate

... continued on page 4, column 1



... continued from page 3, column 3

requires me to use the cost approach, this would not be my preferable method. First, because I'm not in daily contact with prices of construction materials (a cost per square metre would be too simplistic, although widely used), technologies, or volumes. Second, it would not be easy for me to spot a crack in the foundation of a building and translate it into a depreciation amount (again, a depreciation calculated as a percentage of age to economic life would be superficial, although widely used). This discomfort in applying properly the cost approach is due to my lack of full knowledge about the subject matter a civil engineer typically has. Therefore, I ask them for help, if needed.

“The same valuation approaches are used for all asset categories – the difference is in the way they are applied through valuation methods. However, these valuation methods are not always the joy of valuers, depending on their university education.”

Another area with a different focus between the real estate valuer and business valuer is the market research and investigation. Let us consider a tyre manufacturing plant. We have engaged real estate valuers for the land and buildings and business valuers for the overall enterprise. The real estate valuer will search the local market for similar buildings being recently sold or leased and price trends, and/or what would be the alternative use of the subject buildings in case the company goes bankrupt and cannot continue with the same business.

The business valuer instead has a different focus – he/she will search the

market to understand what is the outlook of the car industry. This means analysing the consumer spending behaviour, the competition in the local market or globally, both for the car brands and tyres, expected future prices of different commodities such as oil and electricity, etc. Although this analysis can certainly be done by a real estate valuer, I would not expect him/her to produce the same results as a business valuer should, simply because the real estate valuer does not have the same expertise to do it.

I regularly teach business valuation and real estate valuation. I have seen real estate valuers (mainly civil engineers and architects) struggling during business valuation courses due to a lack of knowledge in accounting and finance. I have also seen them in real estate valuation courses having difficulty to understand and properly apply the profit method. This is because accounting and finance is not in the DNA of an engineer, unless he/she studied it separately. In the same way I have seen accountants with a certain degree of difficulty in real estate valuation courses, when technical matters, such as construction materials, technologies, etc., are discussed.

The business valuation profession is far more dynamic than the real estate one. Valuation methods and procedures in real estate were established a long time ago and the main difference comes from the fluctuations in the real estate market. On the contrary, business valuation is a young profession. Many of the topics I was taught back in 2000-2004 are being questioned. Control premiums back then were given and accepted without much question, but now, new evidence indicates that the premium paid in a transaction reflects more the synergy than the attributes of control. Size premiums, discounts for lack of

marketability, just to name a few, are among other topics on which business valuers have different views. This is all because stock markets are developing every day, not only in the USA, which continues to remain the biggest one, but also in other countries around the world, including the Central European region. Therefore, business valuers never stop learning if they want to stay up to date.

“Valuation methods and procedures in real estate were established a long time ago and the main difference comes from the fluctuations in the real estate market. On the contrary, business valuation is a young profession.”

I preferred to write this short article in first person, because this seemed to me the best way to explain how I feel if I act as real estate valuer, or business valuer. It seems to me I have two hats. The shape may not be so different, but the colour certainly is, and one can spot the difference from a distance. No-one makes these hats for you – you have to tailor them yourself. The fact that you get some training in tailoring does not mean your hat will look nice. You have to do them again and again, correcting errors and imperfections until you find the ones that best suit you. At the beginning you colour them black and white, but as you improve the shape, the colour as well develops to something in between, i.e. neither white, nor black, but certainly not the same colour! This is the story of our life, anyway, in valuation or elsewhere. ●

Anton Lezhja ASA MRICS CF is Chair of the International Institute of Business Valuers.

Waste to energy – a valuer's perspective



The valuation of any property asset needs to reflect the market in which it sits, but the more specialised assets present the valuer with potentially difficult issues to resolve.

“Waste” and “energy” are at the forefront of the current green agenda debate. How should we effectively and environmentally dispose of our waste? And energy production and consumption has become

an emotive subject.

Let us take just a step backwards for a moment. Industrialisation and urbanisation resulted in cities growing rapidly, overwhelming primitive waste disposal. In London, the Metropolitan Board of Works was established and the Public Health Act 1875 imposed a duty to deposit waste in a weekly bin collection for disposal – the “dustbin” was created. Move forward some 150 years and we still rely on the bin collection but the volumes and types of material have changed radically. It is

estimated that in the USA, an average of 2.7 pounds of waste was discarded in 1960 and now, in 2019, it amounts to some 4.4 pounds – per day! That equates to around 250 million tons of waste per annum.

Historically, disposal relied on a number of methods, and although the first incinerator was built way back in 1875 in Nottingham – for many years, most waste went to landfill. Technology and environmental expectations have moved on,

... continued on page 5, column 1



... continued from page 4, column 3

and in today's world, we are fortunate to be able to employ a range of processes and methods of disposal, hopefully limiting environmental damage.

Current waste disposal methods cover a wide range from the simplest waste tipping to sophisticated high-tech incineration. These assets need to be valued for a variety of purposes – annual accounts/business rates/capital gains tax/disposals, etc.

“Technology and environmental expectations have moved on, and in today's world, we are fortunate to be able to employ a range of processes and methods of disposal, hopefully limiting environmental damage.”

The concept of “energy from waste” might include (amongst others) waste incinerators generating electricity, extraction of landfill gas or biochemical conversion (e.g. bio-gas from anaerobic digestion). And as an ancillary part of these processes, the sorting of waste products has become highly sophisticated and mechanised, with plant able to sort bagged products into classes and categories of waste products – so-called “MRFs” (materials recycling facilities).

There are a wide diversity of specialised structures, plant and equipment involved in all these processes. These are highly capital-intensive pieces of investment with anticipated lives in most cases of 30 years plus. The market for such real estate is narrow and limited – often involving company acquisitions and disposals rather than site-specific transactions. What valuation methodologies can be satisfactorily and reliably employed in the absence, in most cases, of reliable market rents or capital transactions?

Waste incinerators/electricity generation

Simply, the process involves burning waste in a boiler, producing steam to drive turbines generating electricity. This has become an attractive sector, given the revenue streams from sales of electricity to the grid. Although revenue-producing, the custom and practice for accounts and business rates valuations is to rely on the “**method of last resort**” – a cost-based assessment adjusted for age and obsolescence factors and any inherent disabilities. In assessing for business rates in England and Wales, the application of statute (the Plant and Machinery

Regulations) will potentially exempt parts of the premises from assessment. In addition, the certification of parts of the premises as a combined “**heat and power**” scheme will potentially ameliorate part of rate liability.

However, adopting a cost-based approach does not always represent “**Market Value**” – the valuer's conundrum of “**does cost equal value**”? Should a revenues-based analysis be undertaken, and if so, over what period should “**fair maintainable trade**” be focused? Energy costs can vary widely from year to year and have a profound effect on revenues and, ultimately, profit.

The waste authority undoubtedly saves on the imposition of “**landfill tax**” if waste goes into the ground – and the sale of electricity produces a reliable revenue stream. But it is uncertain whether such an equation results in a sufficient “**return on capital invested**” – given a typical plant burning some 350,000 tonnes of waste producing 25mw electricity and costing some £250 million. Most facilities are part of a larger “**waste management**” contract with a life of 20 years plus, to secure the necessary substantial investment.

There are around 50 plus such facilities that are currently assessed for business rates in England and Wales, with individual Rateable Values in a range up to £5.5 million (producing an annual business rate liability of some £2,775,000).

“What are appropriate factors to depreciate? Life expectancy of these hard-worked plants is likely to be around 30 years, but at least one is around 50 years old. Such adjustments can produce wide variations in the final valuations.”

The factors used to adjust cost-based valuations come under close scrutiny by the Valuation Office Agency (VOA) – business rates – and auditors (annual accounts valuations). What are appropriate factors to depreciate? Life expectancy of these hard-worked plants is likely to be around 30 years, but at least one is around 50 years old. Such adjustments can produce wide variations in the final valuations.

Landfill gas

Since the 1980s, the extraction of landfill gas has become common practice, not only to supply generators but also with the advantage of controlling methane gas emissions. The system relies upon a network of collection pipes and wells sunk

into mature landfill sites, collecting and compressing the gas for use (as on one site to fire ovens making biscuits!) either/or generating plant. Given that the output of gas is measurable by calorific value, it is possible to value either on an annual basis the output based on a “**Royalty Rate**” or a revenues-based approach. Where is the evidence derived from to apply a Royalty Rate? There is some limited open market evidence of transactions, but, given the niche market, they may not be “**arm's length**”. As an interesting issue – in valuing for business rates purposes, when one of the first large sites came on stream in the 1980s, there was a dispute as to whether “**landfill gas**” was defined as a “**mineral**” for business rates purposes. Legislation permits a 50% “**allowance**” for mineral assessments – and the VOA finally conceded that LFG was indeed a “**mineral**”.

Biochemical conversion

There are a number of schemes adopting chemical conversion – popular within the agricultural sector – involving the storage, treatment and conversion of animal waste into gas which can be sold or used for power generation. The value will be determined by the plant and equipment employed and likely to be valued on a Depreciated Replacement Cost or Contractor's Basis.

In conclusion, valuing any specialised asset requires particular care, given the limited evidence available – a thorough understanding of the processes and plant is essential. But in an ever more environmentally conscious world, valuers will find an increasing number of these premises to value. ●

Iain Dewar is Senior Partner with Wilks Head and Eve LLP, London.

