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Conference Paper

CLASSIFICATION CRITERIA USED AS BASIS FOR AN EFFECTIVE MUNICIPAL PROPERTY MANAGEMENT

51st Congress of the European Regional Science Association: "New Challenges for European Regions and Urban Areas in a Globalised World", 30 August - 3 September 2011, Barcelona, Spain

Provided in Cooperation with:

European Regional Science Association (ERSA)

Suggested Citation: Constantin, Daniela et al. (2011) : CLASSIFICATION CRITERIA USED AS BASIS FOR AN EFFECTIVE MUNICIPAL PROPERTY MANAGEMENT, 51st Congress of the European Regional Science Association: "New Challenges for European Regions and Urban Areas in a Globalised World", 30 August - 3 September 2011, Barcelona, Spain, European Regional Science Association (ERSA), Louvain-la-Neuve

This Version is available at:

<https://hdl.handle.net/10419/120317>

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**The 51st Congress of European Regional Science Association – Barcelona, Spain,
August 30 – September 3, 2011**

CLASSIFICATION CRITERIA USED AS BASIS FOR AN EFFECTIVE MUNICIPAL PROPERTY MANAGEMENT

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Introduction

For many years the issue of real estate management in private sector used to benefit from a much bigger attention compared to the same issue in the public sector, despite the importance of the latter for a proper development of urban systems.

However, in the last decades a significant number of municipal governments have become interested in applying the strategic municipal property management, able to address their real estate “portfolio” in a dynamic vision. It implies the acceptance of the idea of changing the destination of this portfolio in order to find a rational balance between the needs for property for own use, social uses and as investment.

The highest interest in coping with this challenge has been noticed in US, Canada, Australia, New Zealand, UK, etc. Not surprisingly, it is these countries that the most significant studies that can be found in the international literature on this subject come from (e.g. Kaganova and Nayyar –Stone(2000), Jolicoeur and Barret (2004), Musil (2006), RTI International (2006)).

The public property management should be much more developed by the municipal governments in the transition countries as well, considering that they are major holders of urban real estates. In such a context the surplus real property might be a good response to the acute need of local sources of revenues.

Nevertheless, “in transition and developing countries municipal asset management is non-existent or embryonic, and asset management decisions continue to be made in a non-strategic, ad-hoc manner” (Kaganova and Nayyar-Stone, 2000, p. 324).

Hence, the importance of all projects aiming to provide the municipal government with useful tools for public property management. Some results of one of these projects, namely the project entitled “Municipal Property Management on South-Eastern Cities” (PROMISE), funded by the ERDF under the South-East Europe Territorial Co-operation Programme, are to be discussed in this paper.

One of the core components of an effective and accountable municipal property management system is the classification of the available real assets, as a basic step for designing a long-term strategy for each class of properties. Therefore the PROMISE project has established as one of its main goals the development of classification criteria for municipal real property. In order to reach this goal, the most relevant international literature has been reviewed, so as to offer the necessary conceptual framework as well as an image on the good practices for various countries. It has been followed by an inquiry into the content of the International Public Sector Accounting Standards, helping to point out the most frequently used categories of real assets in the public sector. Finally, two case studies have been undertaken in Bulgaria and Romania, showing a particular concern with the correspondence between the destination of each property and its influence on the expenditures and revenues in local budget. In this paper the Romania’s case is discussed.

From the very beginning it should be mentioned that the meaning given to “classification” is that of organization or systematic grouping of varied items into mutually exclusive but related classes, so as to ensure the most effective and efficient use (Merriam-Webster’s Dictionary, Business Dictionary).

It should be also emphasized that there is a large variety of the quasi-equivalent terms, formulations employed for addressing municipal property, such as: asset, real property, real estate property asset, real property asset, item, entity, etc. In our paper almost all these terms can be found. They have been used in order to ensure a higher flexibility and an easier connection with the rich international “language” used in this field.

Classifications of municipal properties identified in the international literature

In strategic asset management, municipal facilities management departments have to play an increasing role so as to provide the appropriate framework for real property assets to be used in accordance with criteria relating to an efficient, effective and economical service delivery. These departments have to adopt an objective, rational and empirical approach, to organize balanced consultations with all stakeholders, so as to find those solutions able to meet in the best way the financial and service delivery needs of the municipality. Thus, asset management appears as an integral element of municipal strategic planning, requiring an appropriate placement, resources and priority for success (Jolicoeur and Barret, 2004).

The survey of the international literature, combined with the description based on the International Public Sector Accounting Standards and the good practices identified in various countries have suggested a series of classification criteria useful for the purposes of our project.

One of the most frequently used classification is based on **physical characteristics** of the properties, resulting in three basic categories: *buildings, infrastructure assets and land* (RTI International, 2006).

The buildings may be used for administrative purposes, the rendering of services, and for housing purposes. The infrastructure assets usually include systems for the power and water supply, roads, bridges, and others. Land lots are properties which could be put to either permanent or temporary use, such as parking lots and parks. For each property part of the asset could be fixed as a separate object, for instance, water pumps, elevators for buildings, etc.

Another widely employed classification categorizes the public real estates by **their use (functional purpose)**, as follows: *administration use, commercial, business / investment use, social use*. This classification usually assigns different financial goals to each class of assets, as proposed by the so-called “Denver model”, elaborated by Utter (1989) and further adapted by Kaganova and Nayyar-Stone (2000). A version of this model is presented in Table 1.

**Table 1. Basic Classification of Local Public Property
(The Modified Denver Model)**

Category	Real Estate Types	Financial Goals
Governmental use (mandatory functions)	City hall, police stations, local public hospital, etc.	Maximize efficiency, minimize costs
Social use (discretionary functions)	Public housing, parks, etc.	Quantify and minimize subsidy
Surplus property	Investment property, remnants from various sources	Maximize financial returns

Source: Kaganova and Nayyar-Stone (2000), p. 316, adapted from Utter (1989).

Derived from the above classification, if the potential for the utilization of properties for commercial or other purposes is considered, two groups result, namely *properties used by the municipality and commercial properties*.

The properties used by the municipality are those which are necessary for local government to perform its functions. They may include municipal administrative buildings, police department buildings, health centers, water supply, parks, roads, zones for public parking, the right of transit, transport terminals, and others.

The commercial properties are those which are offered for lease and could be leased or sold for commercial purposes. Examples in this respect are office buildings, land lots for the rendering of commercial services, sport facilities, parking lots.

In various studies relating to municipal property management have identified two groups of municipal real properties, namely traditional types of property (land, municipal housing, buildings for public use) and free property (Kaganova and Nayyar-Stone, 2000).

The properties that are defined as free property are normally those which do not serve the purposes of the performance operational management functions or the public and social services rendered by the municipality. The free properties may have a mixed composition and origin and in terms of functional purposes include two groups: property used for investment purposes; and properties without a deliberate use.

The classification of municipal property, based mainly on **financial purposes**, is a key factor for its effective management. Based on *the concept for a new public management*, the classification system categorizes real estate municipal property into three groups: ***properties used by local government, properties that serve social needs and free properties***, and defines the different financial purposes of each category of properties.

If necessary, the grouping of property may take into consideration the legal restrictions with regard to some types of property.

The financial goals of maximizing efficiency and cutting costs for the *properties which are directly used by local government* may be achieved by: raising the efficient use of the properties; the decreasing of spending; the establishment of municipal offices services in functional zones; the evaluation of spending and the benefits for the purpose of the best possible utilization of the properties.

The properties used for the rendering of social services encompass those used to achieve the social goals of local government. They are usually put to the best use (for instance, social housing). The financial goal of these assets is to calculate and reduce the maintenance costs, which could be achieved by: the presentation of real expenditures in order to facilitate the best decision making; the creation of a program with alternative measures to reduce maintenance costs.

The free properties are those which are not necessary for the performance of the functions of local government or the implementation of social programs. They are used as a source of revenues by leasing or sales. The purpose of the management of such properties is to increase the return on investment of these assets and to exercise control over spending. This goal may be achieved by: the lease of the property in order to generate repetitive revenues; the sale of the property in order to generate one-lump revenues and imposing taxes on the property; the reduction of the costs for the maintenance of the property, in case it could not be leased or sold.

In addition to the above classification for financial purposes, a classification based on **the way of acquisition, holding and disposition** is also employed, as suggested by Kaganova and Nayyar-Stone (2000). For example, for the way of property acquisition the following are considered: nationalization, transfer from higher levels of government, purchase from private parties, exchange with other public agencies, etc. Holding considers: own use by governmental departments and agencies, lease to the private sector, concession to private sector, used as a

collateral for local government borrowing, etc. Disposition may refer to sale and privatization to private parties, restitution, etc.

The classification of municipal property on the basis of the functional and financial purposes can be used to raise the efficiency of collecting information and reporting, as the different categories of property may require different information. Its advantage is that it can contribute to substantiating a long-term strategy for each category of property and, thus, it is an important factor for the effective management of the municipal property portfolio.

Classifications employed in Romania

In order to successfully apply the classification of municipal property, a wide range of practices and competences of local government in the different countries must be taken into consideration. This variety is determined by the specific legal and institutional framework, the models of administrative and territorial systems in place, legislation and the regulatory framework. The specificity of the municipal property in the European countries determines the goal orientation of local government and the applied management practices.

Based on these considerations, in this part of the paper the application of the classification criteria for the municipal property management is discussed, based on a case study in Romania.

In the case of Romanian public properties a series of legal acts can be used in order to classify them (i.e. to divide into groups according to various criteria), such as: Romania's Constitution, Accounting Law No.82/24.12.1991, Law No. 213/17.11.1998 regarding the public property and its legal status, Law No. 273/29.06.2006 regarding local public finances, Government Decision No. 548/8.07.1999 regarding the technical norms for public goods inventory at county, municipality, town and commune level, Government Decision No. 3471/25.11.2008 regarding the re-evaluation and amortisation of public institutions' patrimony goods, Government Decision No. 2861/9.10.2009 regarding the inventory organising and performing for public capital and debts, The Fiscal Code – Title IX.

The resulted classifications are presented below.

In accordance with the **physical characteristics of the properties**, *buildings* can be:

- building with reinforced concrete frames or with exterior walls made of burnt brick or any other materials resulted from heat and/or chemical treatment;

- building with exterior walls made of wood, natural stone, unburnt brick, or any other materials non treated thermic and/or chemical;
- annex building with reinforced concrete frames or with exterior walls made of burnt brick or any other materials resulted from heat and/or chemical treatment;
- annex building with exterior walls made of wood, natural stone, unburnt brick, or any other materials non treated thermic and/or chemical.

Land can be:

In town: arable land, pasture, grassland, vineyard, orchard, forest or other forest land, land with water, roads and railways, unproductive land.

Terrains: land with buildings, arable, pasture, grassland, harvest vineyard, harvest orchard, land with water (incl. land with fisheries arrangements), roads and railways, unproductive land.

The functional purpose of the municipal property. When efficiently exerting the right of municipal property it is possible to obtain a good balance between the continually evolving requirements of the community, its evolution and modernisation, the social and economical status, observing the laws of the country, taking into consideration the following aspects:

- obtaining a balanced regional development by ensuring the consistency between national and regional development policies;
- providing the physical foundation of local autonomy, ensuring the due rights of local communities and developing the juridical, regulative and institutional frame adequate for the principles of decentralization and local autonomy;
- providing the jurisdiction transfer towards local public authorities and strengthening their administrative capabilities;
- drawing a set of fair and just criteria (the size of the administered territory, population size and requirements, local financial resources, average income per capita) seeking to establish the size of the population included in such a territory in order to manage the municipal property;
- the assets must not get lost or damaged, must be properly maintained in order to preserve and keep them for future generations;
- they must bring benefits to the community;
- they must bring profits that will cover the expenses required for their maintenance and even new investments.

Expenditures and revenues. According to the law, local governments are given financial autonomy and, as a consequence, adopt their own budget which is independent and distinct from the state budget.

Expenditures can come from the payment of property debt and from public acquisitions made by the municipality, namely:

- a) The debts of the administrative -territorial units consist of an integral part of its heritage and represent the obligations with patrimonial feature (financial), which are assumed by the local authorities, under the law, toward certain public and private law subjects in the process of achieving its statutory powers on behalf of, interest and benefit of administrative territorial unit that they represent.
 - Can be considered as debts of administrative-territorial units only the economic obligations (financial) that are strictly defined and recognized as established by law;
 - Territorial-administrative units are responsible for its debts (obligations) exclusively with assets that belong with right of municipal ownership;
 - The payments are made under the local government decision deliberative from the revenue account and / or financial resources unaffected and available of local budget and / or transfer of assets account, in accordance with law and the terms and conditions previously approved by its creditors;
- b) Public procurement is one of the main ways by which local governments procure goods, works or services for the needs of local communities. The main goal of procurement is efficient and transparent use of means from the administrative-territorial units' budgets.
 - In the procurement process local authorities have the capacity of a contracting authority.
 - Object of the public procurement contract may be different categories of goods, services and works procured by local authorities in order to meet and direct or indirect solve some needs and problems of local public interest.
 - The main method of public procurement is open auction. Other ways of making acquisitions can be used only in cases and conditions included into the law.

Regarding the *revenues*, they may come from concessions and donations accepted by the municipality related to the law, by the transmission of property goods into use belonging to the municipality, for payment.

1. Concession is a legal transaction (contract) whereby certain assets owned by territorial administrative units, public services of local interest and other activities aimed at exploiting goods owned by municipal property, based on the decision of the local public authorities, are transmitted into economic management by paying and on a certain period, to individuals with the legal status of entrepreneurs, under the law. The concession of goods, services and local public activities is based on public auction, under the law.
2. Transmission of municipal property assets into use for payment:
 - Can be sent to individuals of private and public right into possession and use for payment by closing rental or lease contracts, where appropriate and under civil law and the Law on Local Public Administration.
 - Local authorities may send into rental or lease any goods of public property and / or private local, excepting the goods which expressly, by the legal provisions, cannot be transmitted into possession and use toward people of private right.
 - Rental and lease contracts may be concluded, as appropriate, to any person or entity, including those of foreign ownership, by the owner of the property right or administration.
 - Transmission of assets as property belonging to administrative-territorial units in rental and / or lease is approved, as appropriate, by decision of the local council, district or autonomous territorial unit.
 - Rental and lease agreements of assets as property belonging to the administrative-territorial units will include clauses in order to assure the exploitation of rental good, in accordance with its specific and its destination.
 - Providing rental and leasing assets is made by public auction, in accordance with the law and the exceptions provided by law.
 - By exception, the transmission of assets as property of public units by rental and lease may be made by other forms (including, direct negotiations) in the following cases: a) obtaining by individuals or entity, under the law of preferential right to conclude rental or lease contract, b) other cases, provided by law or as local public interest, some assets will be transferable into use to determined individuals and businesses, which exclude the need of

organizing the auction. The local public interest and utility in this case is shown, based on studies and opinions, which are presented to deliberative local authorities prior to the decision on sending those assets in use.

- Revenues obtained from the transmission of assets as property belonging to the administrative-territorial units under concession, lease and rental are made income to the correspondent local budgets.

Exempt from taxes are:

- buildings owned by the state, the administrative-territorial units or by any public institution, excepting the premises which are used for economic activities;
- buildings belonging to the public domain of the state and to the administration of "The Administration of the State Protocol Patrimony", except of the premises which are used for economic activities;
- buildings listed in state or administrative- territorial units ownership in the absence of legal or testamentary owners;
- burial cemeteries and crematoria buildings.

Regarding the lands are exempt from taxes and fees the following:

- any land owned, managed or used by a public body, except of the areas used for economic activities;
- any land owned by the state, the territorial- administrative units or other public institutions, for a building whose owner is any of these categories of owners, unless its surfaces are used for economic activities;
- land corresponding to buildings that belong to state public domain and in administration of "The Administration of the State Protocol Patrimony, except of premises which are used for economic activities;
- lands listed in state or administrative- territorial units ownership in the absence of legal or testamentary owners;
- lands corresponding to burial cemeteries and crematoria buildings.

Public goods can be given, where appropriate, in the administration of autonomous entities, prefectures, central government and local authorities, other public institutions of national or local interest.

The concession or rental of public property assets/ goods is made by public auction, under the law. The concession is a contract under which a person called grantor, offers for a determined period of not more than 49 years, to another person, called the operator, who acts on his risk and liability, the right and obligation to exploit a good, an activity or a public service, in exchange for royalties. Royalty achieved through concessions becomes income to the state budget or local budgets, as appropriate. Its calculation and way of payment are established by ministries or by local public administrative authorities.

In the case of public or private buildings belonging to the state or to the administrative-territorial units, leased, rented, given into administration or into use, where appropriate, to entities, is established a tax on buildings, which represents the tax burden of the leaseholders, tenants, holders of administration or use rights, as appropriate, under conditions similar with the tax on buildings. The same situation is also met in the case of public or private state property on lands.

Local councils, the General Council of Bucharest Municipality and county councils, when appropriate, may establish fees for temporary use of public places and for visiting the museums, memorial houses, architectural and archaeological monuments and others.

Charges for possession or use of equipment and machinery for obtaining income which use local public infrastructure can be established, within the local area where they are used, even fees for activities with impact on environment.

State and territorial-administrative units can give buildings from their heritage, into free use, on limited term, toward non-profit legal entities, which carry on charitable or public utility activities, or public services.

The financial objectives of municipal property. They refer to:

- strengthening the financial and patrimonial autonomy of local public authorities;
- re-analysing the revenues – expenses system of the municipality, as well as the entire process of drawing, ratifying, managing and executing the local budget.

The financial resources of territorial-administrative units are subject to the Law regarding the local public finances, according to the principle of local autonomy.

The budgetary process and the budgets of territorial-administrative units are independent to one another, as well as to the national budget.

The local public authorities are provided with an own tax system (different to the national one) made up of taxes according to the Law of local public finances. The local taxation system will be scaled to their own competencies provisioned by the Constitution and other regulations.

The local public authorities are also provided with other financial sources, such as: local taxes, revenues obtained by managing the assets of the territorial-administrative unit and revenues coming from services.

Non-fiscal revenues are not included in the estimate regarding general purpose transfers.

The procedures of distributing the local public authorities' own financial resources, as well as any modification brought to the local public finance system must be coordinated with the representative structures of the local public authorities.

The distribution of competencies without granting financial sources is forbidden, these sources being required in order to cover the costs of the transfer.

The criteria used to distribute the financial support awarded by the national government to the territorial-administrative units must be objective and must be determined according to the law.

The nature of the legal relationship between the municipality and its assets. The municipality acts like a real owner, exercising all the ownership attributes, such as possession, use, disposal in the interest and use of the entire community.

Only in the cases stipulated by the law, one has the right to withdraw positively an owner's assets or to ask the owner to associate its assets to the ones belonging to another owner.

As an administrative–territorial unit, the municipality represents a subject to both public and private ownerships. As a holder of public ownership, it possesses and uses assets of the public domain, of local interest. As a holder of private ownership, it possesses, uses and disposes of assets of the local private domain.

According to the local patrimonial autonomy principle, the full and exclusive right of deciding on the assets owned by the administrative–territorial units belongs to the local deliberative public authorities and it cannot be limited or assumed by any other public authority of other level or by other subjects of right.

Central public authorities consult the local deliberative public authorities in the process of elaborating and adopting of the regulatory framework and of any administrative document which concerns or affect the patrimonial rights or interests of the administrative–territorial units.

The state or the territorial-administrative units have the public ownership on assets which are of public use or interest, according to the law or through their nature.

Within the law, the state or the territorial-administrative units have the possession, use and disposition on the assets that compose the public domain.

The public ownership can be acquired naturally, through public acquisitions according to the law, through expropriation for public use cause, through donation acts accredited by the Government, by the county council or by the local council, if the asset belongs to the public domain, by passing a asset from the state's or territorial-administrative units' private domain to their public domain, for a public use cause, through other legal ways. Assets belonging to the public domain cannot be subject to enforcement and collateral cannot be constituted on them.

Also, these are inalienable, subtle and imprescriptible and cannot be disposed.

Public ownership ends if the asset disappears or it passes to the private domain.

The social purpose of municipal property. The municipality will take on certain high risk activities which are essential to the local community and are not subject to the private investors' area of interest, such as scientific research in different sectors. As main characteristics are:

- it ensures public access to certain social needs such as social, health, educational, cultural services, by creating a broad informational system;
- it creates stable and secure jobs, thus contributing to the development of local economy and therefore of national economy;
- it ensures the stability of public offices and it improves personal experience, it oversees the rights and duties of public employees, based on performance and professionalism, given the fact that local authorities have the right to determine the number of employees and the wages within certain budgetary limits;
- it ensures a balanced development of the managed territory, by reducing regional development imbalances by implementing investment projects and by stimulating the growth of disadvantaged regions.

The local public administration has the right to request the transfer of assets located on its territory towards the territorial-administrative unit patrimony in order to be used in the interest of the local community. The main criteria according to which the central public authorities are forced to pass assets from national property to local public property are:

- objects used for social-cultural reasons, communal, commerce and services, transport and construction reasons – used mainly by the population and enterprises located in the region where they provide the respective services (works), excepting objects having a national significance, the activities related to those being subject to the national budget;
- objects used in telecommunication and transport, roads – their location on the respective territory, excepting telecommunication items of national operators, national roads, railway, air and water transport and national pipe-lines;
- objects used in industry – used mainly by the population and enterprises in the region where the production is manufactured.

Economic performance of the properties. It is governed by the following rules, principles:

- the elimination of political reasons for granting financial resources the local authorities;
- the adoption of a new system regarding local public finances, in order to re-analyse the revenues – expenses system, as well as the entire process of drawing, ratifying, managing and executing the local budget;
- creating regulations in order to be able to quantify local patrimonies, by creating a unitary and general registry of municipal property;
- adopting certain development strategies in order to improve territorial planning and investment localisation;
- ensuring the efficient use of funds in regional projects according to the financing decisions of authorized authorities and with the observance of legal standards.

Features of evaluation and assessment criteria in Romania

In European Union the International Valuation Standards (ISV) have been applied since 2003. Also, in Romania, there are several methods recommended to be taken into consideration when evaluating an estate property, following the recommendation provided by the National Evaluators Association in Romania (ANEVAR, 2004). These standards identify the three main generally accepted valuation approaches. Variations or adaptations of these approaches are used in the valuation of most types of asset.

Markets rarely operate perfectly with constant equilibrium between supply and demand and an even level of activity, due to various imperfections. Common market imperfections include disruptions of supply, sudden increases or decreases in demand or asymmetry of knowledge

between market participants. Because market participants react to these imperfections, at a given time a market is likely to be adjusting to any change that has caused disequilibrium. A valuation that has the objective of estimating a price in the market has to reflect the conditions in the relevant market on the *valuation date*, not an adjusted or smoothed price based on a supposed restoration of equilibrium. If the *basis of value* is not *market value*, entity specific factors may be considered. If the objective of the valuation is to determine the value to a specific owner, entity specific factors are reflected in the valuation of the asset.

One or more valuation approaches may be used in order to arrive at the valuation objective defined by the appropriate *basis of value*. The three main approaches described and defined in this standard encompass all the significant methods used in valuation. They all are based on the economic principles of price equilibrium, anticipation of benefits or substitution. The methods used to apply the principles of these three valuation approaches to different asset types are discussed in the relevant standard.

Direct Market Comparison Approach. This is a comparative approach that considers the sales of similar or substitute assets and related market data. In general, an asset being valued is compared with similar items that have been transacted in the market or that are listed or offered for sale, with appropriate adjustment to reflect different properties or characteristics.

Income Approach. The income approach considers the income that an asset will generate over its remaining useful life and estimates value through a capitalisation process. This process applies an appropriate yield, or discount rate, to the projected income stream to arrive at a capital value. The income stream may be derived under a contract or contracts, or be non-contractual, e.g., the profit generated from either the use of or holding of the asset.

Two commonly used methods that fall under the income approach are income capitalisation, where an all risks yield is applied to a fixed income stream, or discounted cash flow where the cash flows for future periods are discounted to a present value. The income approach can be applied to liabilities by considering the cash flows required to service a liability until it is discharged.

Cost Approach. This approach applies the basic economic principle that a buyer will pay no more for an asset than the cost to obtain an asset of equal utility, whether by purchase or by construction. Unless undue time, inconvenience, risk or other factors are involved, the price that a buyer would pay for the asset being valued would not be more than the cost to acquire or

construct a modern equivalent. Often the asset being valued will be less attractive than the cost of a modern equivalent because of age or obsolescence; where this is the case, adjustments will need to be made to the cost of the modern equivalent. This adjusted figure is known as the *depreciated replacement cost*.

Hierarchy of Approaches. Where directly observable prices for identical or similar assets are available at or close to the *valuation date*, the direct market comparison approach is generally preferred. Where this approach cannot be applied reliably because of either an absence of price information or because the asset is unique or has features that make it materially different to other assets of a similar type that are being transacted at or close to the valuation date, the income approach or the cost approach may be more appropriate.

Methods of Application. Each of these principal valuation approaches includes different detailed methods of application. Various methods that are in common use for different asset classes are discussed in the Asset Standards in the 300 series of ANEVAR. The *basis of value* that is required, market practice and the data available to provide valuation inputs combine to determine which method or methods is the most appropriate.

Use of Multiple Approaches and Methods. In some cases it will be appropriate to use more than one approach or method in order to arrive at the valuation estimate, especially where there are insufficient factual or observable inputs to fully support the use of one method. Where alternative approaches and methods are used, these should be weighed and reconciled into a final value estimate.

Valuation Inputs. Valuation inputs refer to the data and other information that is used in any of the valuation approaches described. These inputs may be actual or assumed.

Examples of actual inputs include:

- prices achieved for similar or identical assets;
- actual income generated by the asset;
- the actual cost of an asset.

Examples of assumed inputs include:

- estimated or projected cash flows;
- the estimated cost of a hypothetical asset;
- market participants' perceived attitude to risk.

Greater weight should normally be given to actual inputs; however, where these are less relevant, e.g. where the evidence of actual transactions is stale or the actual cost information historic, assumed inputs may carry greater weight.

The nature and source of the valuation inputs should reflect the valuation objective. For example, various approaches and methods may be used to estimate *market value* providing they are based on market derived data. Direct market comparisons inevitably are market derived. The *income approach* should be applied using cash flows as would be determined by market participants and market derived rates of return. If applying the *cost approach*, construction costs and depreciation should be determined by reference to an analysis of market based estimates of costs and accumulated depreciation.

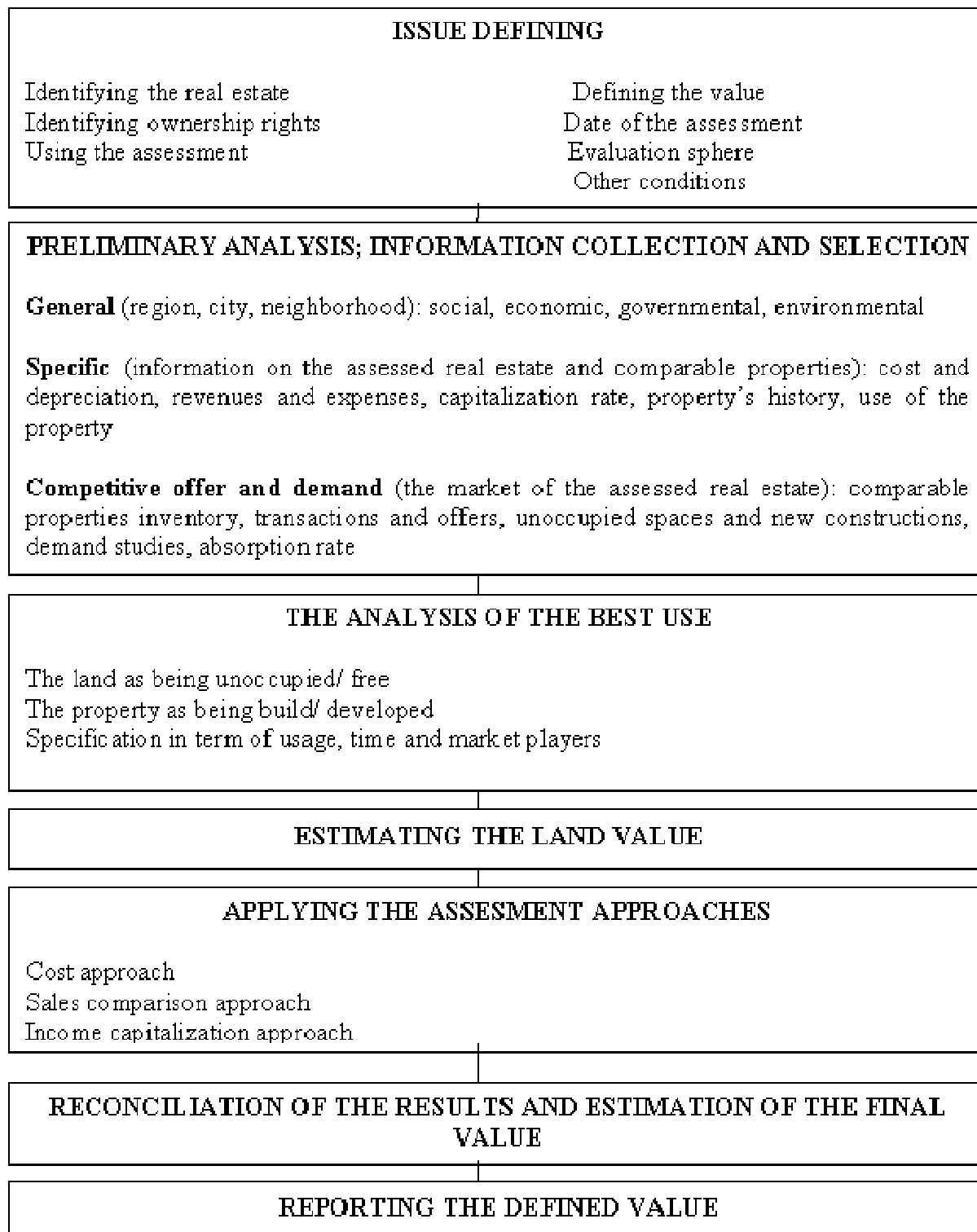
Although data availability and circumstances relating to the market or the asset being valued will determine which valuation methods are most relevant and appropriate, the outcome of using any of the foregoing procedures should be *market value* if each method is based on market derived data.

Valuation approaches and methods are generally common to virtually all types of valuations. However, valuation of different types of assets involves different sources of data that appropriately reflect the market in which the assets are to be valued. For example, the underlying investment of *real estate* owned by a company will be valued in the context of the relevant *real estate* market in which the *real estate* trades, whereas the shares of the company itself will be valued in the context of the market in which the shares trade.

In **Romania** the process of evaluation is based on defining the major issues and on planning the necessary activities in order to solve the identified problem. The necessary data for evaluation are gathered, sorted, analyzed, commented and refined for a proper estimation of the property value. The process of evaluation in Romania is based on different steps; their number depending on the nature of evaluation and accessible information. The above mentioned steps are outlined in Figure 1.

Further on, a **series of indicators** used in the process of real estate property assessment in Romania is presented. These indicators were extracted from an assessment handbook of ANEVAR (2004), a relevant institution for property assessment in Romania. The base of indicators selection was represented by the methods and techniques of real estate property evaluation.

Figure 1. Property assessment process in Romania



Source: The National Evaluators Society in Romania, *Real Estate Evaluation Handbook*, ANEVAR Collection Library, 2004, Annex 1, p.6 (translation from Romanian)

The methods used in the Romanian practice consist of the following: direct comparison method, cost method and yield method.

- **Direct comparison method** is based on a process in which the market value estimation is made by market analysis in order to identify similar properties and then, the identified properties are compared to the one in assessment.

Potential indicators for property evaluation can refer to: price on square meter, capitalization rate, transmitted ownership rights, financing conditions, selling conditions, market conditions, location, physic characteristics, economic characteristics, usage, property access, governmental restrictions, environmental conditions, infrastructure development, usage coefficient, available surface for renting / concession / selling, etc., expenditure coefficient.

- **Cost method** is also based on comparison. The building costs of a property are compared to the value of an existing property or to the value of a similar building under development. The method underlines the relationship between the value and costs.

Potential indicators for property evaluation can refer to: land value, absorption rate, the level of exploitation expenses, long-term fructification rate, quantifying the risk associated to the best usage of the property, development normative, environmental impact, property's dimensions, property's surface, geological structure of the land, available utilities corresponding to the property, financial feasibility, market value, direct costs, indirect costs.

- **Yield method** considers the property as being a profit generator investment.

Potential indicators for property evaluation can refer to: income corresponding to the property, profit corresponding to the property, income rates, profit rates, return of capital.

Concluding remarks

In the analysis of municipal properties (assets), classification and assessment (evaluation, ranking) represent two distinct phases, which occur logically one after another.

The classifications serve for analyzing the nature and content of properties, by grouping them using different criteria, thus representing a preliminary step for performing realistic assessments.

In Romania, the process of evaluation is based on defining the major issues and on planning the necessary activities in order to solve the identified problem. The necessary data for evaluation are gathered, sorted, analysed, commented and refined for a proper estimation of the property

value. The process of evaluation in Romania requires several steps, their number depending on the nature of evaluation and available information. In most of cases the steps refer to: issue defining, preliminary analysis, gathering, and selection of information, analysis of the best use, estimating the land value, applying the assessment approaches, reconciliation of the results and estimation of the final value, and reporting the defined value.

In Romanian practice, there are a series of methods used for real estate property assessment, which can also be used for municipal property assessment. These methods refer to direct comparison method, cost method and yield method. Direct comparison method is based on a process in which the market value estimation is made by market analysis in order to identify similar properties and then, the identified properties are compared to the one in assessment. Cost method is also based on comparison. The building costs of a property are compared with the value of an existing property or with the value of a similar building under development. The method underlines the relationship between the value and costs. Yield method considers the property as being a profit generator investment.

Acknowledgement. This paper presents a part of the contribution delivered by the research team of the Academy of Economic Studies of Bucharest (Project Partner 2) to the project “Municipal Property Management in South-Eastern Cities (PROMISE)” - funded by the European Fund for Regional Development within the South-East Europe Transnational Co-operation Programme. The cooperation with the SEED Centre of the University of Thessaly, Greece as Lead Partner as well as with the University of National and World Economy, Sofia, Bulgaria, also partner in this project are gratefully acknowledged.

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