# Income Approach to Value Problems and Answers

2023 Level I Tutorials

Development of Allowable Expenses

Given below is the statement of expenses for a business as prepared by the owner's accountant. They are actual bank withdrawals and are assumed to be correct. In your analysis of the statement for appraisal purposes, you have decided that some items can be used as stated, others need to be eliminated, and some need to be pro-rated. Indicate with an "X" which items you would use as stated, pro-rated (over more than one year), or would eliminate from your reconstructed operating statement.

| | | As Stated | | Pro-Rate | | Eliminate |
|---|---|---|---|---|---|---|
| A. | Management Fees | | | | | |
| B. | Advertising | | | | | |
| C. | Maintenance Personnel Salaries | | | | | |
| D. | Maintenance Personnel Benefits | | | | | |
| E. | Debt Service on Mortgage | | | | | |
| F. | Water and Sewage Fees | | | | | |
| G. | Electricity | | | | | |
| H. | Gas for Heating | | | | | |
| I. | New Roof | | | | | |
| J. | Miscellaneous Repairs | | | | | |
| K. | Supplies | | | | | |
| L. | Casualty Insurance--3 year policy | | | | | |
| M. | Liability Insurance | | | | | |
| N. | Snow Removal | | | | | |
| O. | Income Tax | | | | | |
| P. | Donation, Christmas Gift Expense | | | | | |
| Q. | Real Estate Taxes | | | | | |

## Development of Allowable Expenses

Indicate with an "X" which items you would use as stated, pro-rated (over more than one year), or would eliminate from your reconstructed operating statement.

| | | As Stated | | Pro-Rate | | Eliminate |
|---|---|---|---|---|---|---|
| A. | Management Fees | X | | | | |
| B. | Advertising | X | | | | |
| C. | Maintenance Personnel Salaries | X | | | | |
| D. | Maintenance Personnel Benefits | X | | | | |
| E. | Debt Service on Mortgage | | | | | X |
| F. | Water and Sewage Fees | X | | | | |
| G. | Electricity | X | | | | |
| H. | Gas for Heating | X | | | | |
| I. | New Roof | | | X | | |
| J. | Miscellaneous Repairs | X | | | | |
| K. | Supplies | X | | | | |
| L. | Casualty Insurance--3 year policy | | | X | | |
| M. | Liability Insurance | X | | | | |
| N. | Snow Removal | X | | | | |
| O. | Income Tax | | | | | X |
| P. | Donation, Christmas Gift Expense | | | | | X |
| Q. | Real Estate Taxes | | | | | X |

# Income Approach

- At this time, please go back to the Income Approach PowerPoint and resume on slide #95.

## Income Approach
## Problem # 1
## Determination of Net Operating Income

You are trying to determine the value of a small retail center containing 4,500 square feet of Net Leasable Area. There are three leasable spaces in the building, and at present two of the spaces are leased. You have determined the following information:

1.) Market rent for this type of space is $22 per square foot.
2.) The owner has $3,000 per year in miscellaneous income.
3.) The market vacancy rate is 4% and the market collection loss rate is 1%.
4.) Operating Expenses from the reconstructed operating statement are $30,500.
5.) The Reserve for Replacements is $5,000.

Determine the Net Operating Income (NOI) for the subject property.

| | |
|---|---|
| Potential Gross Income (PGI) | |
| Vacancy and Collection Loss | |
| Miscellaneous Income | |
| Effective Gross Income (EGI) | |
| Operating Expenses | |
| Reserves for Replacements | |
| Net Operating Income (NOI) | |

## Income Approach
## Problem # 1 Answer
## Determination of Net Operating Income

| | |
|---|---|
| Potential Gross Income | $99,000 |
| Less: Vacancy and Collection Loss | ($4,950) |
| Add:  Miscellaneous Income | $3,000 |
| Effective Gross Income | $97,050 |
| Less: Operating Expenses | ($30,500) |
| Less: Reserve For Replacements | ($5,000) |
| Net Operating Income | $61,550 |

| | |
|---|---|
| Net leasable area of 4,500 Square feet times $22/Square Foot | $99,000 |
| Vacancy loss rate of 4% plus Collection loss rate of 1% times PGI | ($4,950) |
| Add miscellaneous income (given) | $3,000 |
| Effective Gross Income (EGI) | $97,050 |
| Less expenses (given) | ($30,500) |
| Less reserves for replacements (given) | ($5,000) |
| Net Operating Income (NOI) | $61,550 |

# Income Approach

- At this time, please go back to the Income Approach PowerPoint and resume on slide #99.