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## Valuation Of Immovable Property For Mortgage

Land and buildings are real wealth of the nation because they are the primary assets which are instrumental in generation of nation's wealth.

Without financial support of financial institutions, a nation cannot create wealth and do real progress. Collapse of major financial support means collapse of NATION'S Economy.

### Abstract:

In the realm of secured lending, property valuation serves as a foundational element in risk assessment and loan sanctioning. Accurate and professional valuation not only safeguards financial institutions from overexposure but also instills borrower confidence and regulatory compliance.

This article presents a comprehensive overview of the valuation process for mortgage purposes, covering principles, methodologies, influencing factors and challenges. The aim is to provide valuation professionals, bankers, regulators, and academics with a consolidated reference to enhance valuation practices and promote informed decision-making in mortgage lending.

### Introduction:

It is customary to advance finance for development by accepting real property of the borrower as security. Real property is one of the most preferred forms of collateral in the financial system. As immovable property is taken as security against the loan advances, it is very important for the money lending institution to know real market

worth of the security pledged for mortgage, at the time of loan advances. Real issue in mortgage against security is therefore valuation of property offered as mortgaged to Bank. We can also say that one of the prime factor for consideration for loan advances to the borrower, would be the intrinsic market value of the security. Valuation, in this context, is not a mere numerical exercise but a crucial component of credit risk management, regulatory compliance, and financial prudence.

The mortgage valuation process aims to establish the fair market value of a property as of a specific date to determine the appropriate loan-to-value ratio and protect the lender's interest. An incorrect or biased valuation can lead to under-lending, over-lending, or increased non-performing assets, severely impacting institutional balance sheets.

Valuers could help financial institutions by giving fair idea of real worth of the property in the market at the relevant period of time.

### **Valuation process:**

#### **To have a value of any property it must have four basic qualities**

- Utility
- Scarcity
- Demand
- Transferability

If property has no use or no utility, no one will want it and hence there will be no demand and no value for such property.

Next quality required for value is that the property has to be scarce in supply. The properties which are available in limited quantity and are not in abundance command high value.

Similarly transferability is essential quality to have value. If ownership of property is not transferable, no Bank would advance any loan to the borrower against non-transferable security. The ownership and possession of the property can be transferred by way of sale, gift, lease, mortgage, will etc. and hence it has a value.

There are innumerable factors which affects the value of the Immovable property in the open market. Increase in F.S.I. can increase value of the land. Increased demand and higher paying capacity of residents would increase value of property. Increased money supply in the market could also increase value of properties in the market. On the other hand construction of fly-over or mono rail in front of the building would reduce the value of property. Bad planning of rooms inside the flat will also reduce the value. Flats on main road would fetch higher price than flats in the by-lane. Properties with clear view fetch higher values. Flats in new building built under Slum Redevelopment Scheme would fetch lower rate. There are endless aspects affecting the value. Broadly all these factors could be classified into following four groups.

- Economic Aspects: Demand and Scarcity, Money supply, Yield rate, Availability of money and credit, and interest rate levels..
- Legal Aspects: Rent Act, Development Rules, Possession, Ownership, Regulation of industries, Environmental protection laws, Zoning and land-use regulation
- Technical Aspects: Type of construction, age, amenities, planning & design.
- Social Aspects: Proximity of civic amenities, School, Garden, Market, Life-style and Living standards, Population growth.

If there is less demand of flats or bungalows in the market, value of flats or bungalows will fall. This has happened in America after collapse of economy in 2008. There were no buyers for the properties of borrowers even at 50% discount in the Public Auction. Demand & Supply is a very powerful market force.

Value changes with legal rights held by the owner in a property. Changes in holding pattern in the property will change the value of the property. A plot may have a value of 50 Lacs when it is freehold, i.e. 100 % rights are held by the owner. However, as soon as said owner leases the plot to lessee on agreed ground rent, value of his ownership rights will get reduced to say 45 Lacs.

Under Transfer of Property Act, owner holds following rights.

- Right to use and enjoy the property permanently.
- Right to Rent, Lease, transfer or Assign the property.
- Right to possession and occupation.
- Right to alienate or destroy the property. (Building can be destroyed)
- Right to Gift or Will or create life interest for anyone.
- Right to develop or permit development of property.

All these rights are called bundle of rights. If owner retains some rights and parts with some other rights, value of property changes.

Renting out the premises to tenant is giving away part of the right viz. occupancy right but continue holding ownership right in the property. Value changes with changes in technical aspects. It is well known that flat with superior specification and amenities fetches higher value in the market as compared to the price of flat having inferior specification and poor amenities. Even planning of rooms inside the flat and outside aesthetics of building also changes value of the property. Value changes due to social aspects. Price of flat in the posh locality is higher than the rate of flat in the middle class locality. If civic amenities are available close by, the value of the property goes up.

Bankers must understand some Valuation Terminology. 'Cost' is not same as 'Value'. Market value is not same as Forced sale value. Similarly Special Value, Prestige value, Potential Value, Sentimental Value, all carry different meaning and each one has different values in the real estate market.

Bankers must also know what the definition of word “Market Value” is. International Valuation Standard Council (IVSC) have defined **“Market Value” in following words. “Market value is estimated amount for which an asset ought to exchange on the date of valuation, between a willing buyer and a willing seller, in an arm’s length transaction after proper marketing, where in the parties had each acted knowledgeably, prudently and without compulsion”.**

This is an excellent definition of ‘value’ and valuer must consider all these aspects stated in the definition, while estimating value.

### **Different Approaches Of Valuation**

**There are three approaches available to value the immovable property.**

- Income Approach: Rental Method, Profit Method, Discounted Cash flow Technique.
- Cost Approach: Land and Building Method.
- Market Approach: Sale Comparison Method, Development Method.

Depending upon the facts and circumstances in each case, the valuer adopts most appropriate method of valuation. Adoption of improper method, would lead to an incorrect valuation of the property.

Normally rented premises are valued by Rental Method.

Bungalows and factories are valued by Land and Building Method.

Flats, owner occupied commercial establishments are valued by Sale Comparison Method.

However, the distinctions between these three methods are not rigid, and overlaps do exist. Values can be worked out by other methods also in certain case. For examples, a palatial bungalow in a small village will have to be valued by rental method instead of Land and building method.

### **Factors influencing Valuation of Property**

**Numerous intrinsic and extrinsic factors influence the value of property which include:**

- Location and Zoning: Connectivity, Centrality, Permitted use.
- Site Characteristics: Shape, Size, Area, Frontage.
- Construction Quality: Specifications, Material used, Age, Maintenance
- Legal Status: Clear title, Encumbrances, Litigation
- Economic Conditions: Inflation, Interest rates, Real estate cycle
- Infrastructure and Amenities: Access to roads, Utilities, Markets, Public transport
- Regulatory Restrictions: FAR/FSI limitations, Master plans, Heritage norms

## Challenges and Risks in Mortgage Valuation

Despite its importance, the mortgage valuation process is fraught with challenges, including issues of Data reliability, Methodological divergences.

Uncertainties associated with economic and policy shifts.

Discrepancies in legal titles,

Pressure from borrowers or lenders to inflate or deflate valuations.

Informal property markets with poor regulatory coverage.

Valuers must navigate these complexities while maintaining independence, neutrality, and adherence to professional ethics. The credibility of the mortgage valuation process rests not only on technical competence but also on the valuer's ability to exercise sound judgment free from external influence or bias. Independence ensures that valuations are not swayed by the interests of lenders, borrowers, or market participants; neutrality safeguards the objectivity of reported values; and professional ethics anchor the entire process within a framework of accountability and public trust. In this sense, the valuer functions as both a technical expert and a custodian of integrity in the financial system.

## Practices for Mortgage Valuation

To maintain credibility and quality in valuation assignments, professionals should:

Maintain independence and confidentiality

Refrain from value manipulation under any influence

Keep updated with legal changes, market trends, and technical standards

Engage in continuous professional development.

Adhering to these practices contributes to the credibility of both the valuation report and the institution relying upon it.

Having learnt most of the basic valuation principles, the banker should never forget most important fundamental principle that what is valued is right of the borrower in the security offered for mortgage. **If there are no rights, there is no value of the property.**

Many valuers are fond of valuing property by averaging out values arrived at by two different methods. Prima facie this may appear to be safe and acceptable as a compromise formula, however, temptation to arrive at an average value should always be scrupulously or strictly avoided because in reality, average never exists.

The mere averaging of two results obtained by quite different base of approach can hardly be said to represent any logical approach.

Bankers also sometimes do this. They average value estimated by two different valuers and adopt the average value as the market value of the security. This is dangerous. This may or may not work.

It is invariably noticed that valuers blindly adopt land values stated in the Ready Reckoner or guide lines tables of stamp authorities, for determining market value of the land. This approach is not only incorrect but very risky. Values stated in Ready Reckoner are average values for whole locality. Land values in locality can be higher or lower than this average rate. It is absurd to think and accept that land values for all types of land in a locality will be uniform. Values are bound to change depending upon characteristics possessed by each piece of land. To adopt figures prepared in valuation guide lines would be dangerous, because they offer no guarantee of truth or correctness of data, not being susceptible to check or verification by a judicial or quasi-judicial process of evaluation of evidence.

A person or institute who uses valuation report of a valuer is many times faced with situation where price of same property, for same date, are estimated at different figures by two valuers. This difference normally should not vary more than 15% to 20%. But we find that in some cases this difference is as high as 100% to 500%. Reasons for this wide difference could be many. Valuers might not have visited the property or they have not done market inquiry or they have not examined all relevant documents of the property. The reason could also be that different methods of valuation are adopted by two valuers and one of the two valuers might have adopted wrong method of valuation. Courts also considered 15% variation as honest difference of opinions between two valuers.

Bankers, could take some precautionary measures as detailed below which may perhaps help them in reducing Bank's NPA. (Non-Performing Assets).

- Bank should take legal opinion on clear title and ownership rights of borrower at initial stage before processing loan application. Borrower's rights in the property must be saleable in the open market. If there are no rights, there is no value.
- Bankers should ask valuer to report two values. Fair market value and Forced sale value. Banker should realize that value of property as on today may not remain same in future when borrower becomes defaulter. Indian economy is not that stable that any valuer or even an expert economist could forecast values after five years. Adequate safety margin (Margin money) should be therefore kept on reported value. When property becomes NPA, fresh report should be obtained from the valuer, before onetime settlement or public auction.
- Never advance loan unless Bank's officer has physically inspected the property offered as security.
- Bankers should resist temptation of pressurizing valuers, for giving favourable report of expected or predetermined values.
- In case of large loan advances say above five crores, Banks should take independent opinion, on property value, from two expert valuers.
- Bankers should not give instructions to valuer on telephone but written instruction is necessary in every case. Valuer should be paid appropriate fees for the valuation work.

- Do not ask valuer of real property to value plant and machinery. Similarly do not ask valuer of plant and machinery to value land and building.
- Give sufficient time say 2 to 3 days to the valuer to submit Valuation Report so that he can scrutinise documents, inspect site and make sufficient market inquiry.
- Appoint only experienced and competent valuers to value the property. All Architects and all Engineers are not valuers. Similarly all retired government engineers are not necessarily expert in valuation. For major valuation assignments, valuation practice of the valuer for a minimum period of 10 years is must. It is better if Banks evolve a system of maintaining separate Panel of senior Valuers on the basis of their past performance with the Bank.
- Property of borrower should be got valued every two years.
- In case of borrower owning running industrial unit, value of his asset as 'Going Concern' i.e. value for "Continued use" should be obtained. Value of such a property as exchange value or its breakup value or its value for alternative use or its value for Highest and Best use should not be considered for advancing loan to running units.
- Reading only concluding para of the Valuer's Report is not sufficient for the Banker. Banker should go through whole report of the valuer including identification statement of the property, assumptions made by the valuer and the methodology adopted by the valuer in estimating market value. Checking and comparing information gathered by Bank's officers with details in valuer's report would minimize fraud cases.
- Banks should organize a continuing education programme every three years for their Panel Valuers.
- Bankers should tell borrowers that Bank would advance loan amount equivalent to minimum price that the property would fetch in the open market less 50%.

Bankers having some basic knowledge of asset Valuation can certainly administer the loan advance in much better manner.

### **Conclusion:**

Valuation of properties for mortgage purposes is a critical function that directly influences lending decisions, financial stability, and institutional risk management. With increasing market complexity and regulatory scrutiny, the role of the valuer extends beyond numerical estimation—it encompasses diligence, judgment, ethics, and a deep understanding of real estate and financial systems.

To meet the growing expectations of lenders, regulators, and stakeholders, valuation professionals must evolve with the times—adopting technology, enhancing transparency, and reinforcing professional integrity. Only then can valuation serve its intended purpose as the bedrock of secure and sustainable mortgage lending.