


Turning Point of Land Evaluation

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Japan has the bitter experience that during its high economic growth period, land prices rose dramatically, stimulating speculative transactions in land. As a result, the National Land Use Planning Law and the Public Notice of Land Prices Law were enacted with the aim of suppressing rises in land prices and discouraging speculative land transactions. The former is a law with strong authority including the constraint of private property rights (approval scheme for transactions), but currently the designation of regulated areas which acts as the grounds for its being set in motion is not being carried out. These seems likely to remain the case in the future barring the occurrence of exceptional situations.

Meanwhile, one of the objectives of the Public Notice of Land Prices Law is to act as a compensation criterion when acquiring land for public use. It also has a certain degree of indirect impact, on the calculation of property tax evaluation. It is also used as an indicator for general land transactions.

In the past, real estate transactions in Japan were carried out targeting land, with the result that the objective of these systems in Japan is to provide an indicator of land prices. In addition, due to the need to provide an exhaustive indicator across the whole country, they are forced to give priority to the balance between points. The same applies to property tax evaluation.

Recently however, transactions for profit-bearing real estate focusing both on land and building are very common, and the pricing of real estate has become increasingly based on capitalized value. This trend has cast a light on the issue of advisability and the future direction of valuations, and the Japanese Association of Real Estate Appraisal has clearly indicated its stance to emphasizing the capitalized value approach.

However, the attitude that the land price is an indicator is unlikely to change immediately, and this is causing various problems. For example, when applying cost and profit analysis at real estate investment, you most likely may find out that the profitability of real estate does not necessarily balance with the property tax evaluation. This is probably caused by the fact that the evaluation based solely on land and on profit from the rent do not correspond. If the market changes evaluation based on profit from the real estate, then the individuality of real estate will have an even greater impact on price, which is likely to result in a change in the balance.

This would also result in a situation that the taxes such as real estate acquisition tax and fixed asset tax may not correspond with the profitability of real estate. These real estate taxes have in some respects been levied targeting the capital gain of real estate, since Japan had enjoyed ever-higher-land price in the past decades. Also, the real estate taxes had been used politically to suppress the boost of land price.

In today's deflationary market, however, there is no danger of a sudden rise in land prices, and the tax bearing capacity of real estate itself is shifting towards profitability centering on income gain. I believe that the real estate taxes and evaluation methods must seriously be revised now when the securitization of real estate is set as one of the governmental policy.