

**COMMON EXAMINATION FOR HOUSE AGENTS**

**PAPER 3**

**PROFESSIONAL PRACTICE AND MANAGEMENT**

Wednesday, 7 Jan 2009

2 ½ hours

100 marks

**Instructions:**

1. Answer any **5 (FIVE)** out of 8 questions.  
(You must not provide answers to more than 5 questions.)
2. Each question carries 20 marks.

**Failure to comply with the above instructions may result in loss of marks.**

Question 1

Each part of this question carries two (2) marks. You are required to indicate the most appropriate answer for each part of this question in the answer script. No marks will be given if the answer is not clearly indicated. If more than one answer is given to any part, no marks will be awarded for that part.

(I) Consider the following statements:

- (i) The characteristics of a real estate market include (a) the non-existence of a central trading place, (b) high transaction costs, and (c) guaranteed capital appreciation.
- (ii) The market rent of a condominium unit is not affected by the state of maintenance of the common areas.

- (A) Statement (i) is correct and statement (ii) is incorrect.
- (B) Statement (ii) is correct and statement (i) is incorrect.
- (C) Both statements are correct.
- (D) Both statements are incorrect.

(II) Consider the following information about a condominium unit: (i) number of bedrooms; (ii) number of occupiers; (iii) size of swimming pool in the condominium project.

The open market value of the property will not be affected by

- (A) (ii) and (iii) only.
- (B) (ii) only.
- (C) (iii) only.
- (D) (i) and (iii) only.

- (III) Consider the following: (i) height restrictions imposed on the site; (ii) land area; (iii) neighbourhood characteristics; and (iv) length of road frontage.

The selling price of a vacant residential site will be affected by

- (A) (i), (ii), and (iv) only.
  - (B) (i), (ii), and (iii) only.
  - (C) (ii) and (iii) only.
  - (D) None of the above answers.
- (IV) Which one of the following statements is incorrect?
- (A) A code of conduct ensures that professional standards are maintained and consumers' interests are protected.
  - (B) Ethical standards are restricted to only those prescribed in the code of conduct of the professional body.
  - (C) One of the factors affecting the highest and best use of a site is the intensity of development that will be approved by the competent authority.
  - (D) None of the above answers.
- (V) Which one of the following statements is incorrect?
- (A) The effective demand for real estate is derived from its attributes of indivisibility, immobility and heterogeneity.
  - (B) Utility and scarcity are two important factors that affect value in exchange.
  - (C) Value in use is often subjective because it may include sentimental value that is difficult to quantify in monetary terms.
  - (D) None of the above answers.

- (VI) Consider the following: (i) age of property; (ii) floor area of property; and (iii) number of beneficiaries in the will.

Under a reverse mortgage, the monthly income receivable by the owner of the property would not be affected by:

- (A) (i) and (ii) only.
  - (B) (i) and (iii) only.
  - (C) (ii) and (iii) only.
  - (D) None of the above answers.
- (VII) Messrs AKC Ltd receives cash of \$4,500 for services rendered to a client. The firm bought \$1,500 worth of stationery on credit to be paid in 3 months' time.

Consider the following accounting entries; (i) debit entry of \$4,500 for the cash account; (ii) credit entry of \$4,500 for the revenue account; (iii) debit entry of \$1,500 for the stationery account; and (iv) credit entry of \$1,500 for accounts payable.

The correct accounting entries to reflect the transactions are:

- (A) (i) and (ii) only.
- (B) (i), (ii), and (iii) only.
- (C) (i), (ii), (iii), and (iv).
- (D) None of the above answers.

(VIII) Which one of the following statements is incorrect?

- (A) During the initial stage of the upswing phase of the real estate cycle, one would not expect to see credit tightening.
- (B) A breach of business and professional ethics is evident in the case of a real estate agent informing potential buyers that the vendor is under severe financial pressure to sell the property.
- (C) The amount of bank loan that will be granted is an important factor to consider when determining which is the most appropriate valuation method to estimate the open market value of a property.
- (D) None of the above answers.

(IX) Which one of the following statements is incorrect?

- (A) Economic obsolescence refers to the decrease in property value arising from wear and tear through usage.
- (B) When the demand of real estate exceeds supply, prices will generally rise.
- (C) Real estate markets are affected by cyclical changes in the economy.
- (D) The factors affecting the supply of real estate include the cost of land and the availability of financing for construction.

- (X) Consider the following: (i) the buyer and seller are willing parties to the transaction; (ii) the buyer and seller have knowledge of market trends; and (iii) the vendor has taken adequate marketing efforts to sell the property.

The definition of open market value takes into consideration

- (A) (i) and (ii) only.  
(B) (i) and (iii) only.  
(C) (ii) and (iii) only.  
(D) (i), (ii), and (iii).

(20 marks)

Question 2

- (a) During 2008, there was a significant drop in the number of residential enbloc transactions. Discuss the factors that could account for this observed trend.

(10 marks)

- (b) Identify five (5) errors in the following Balance Sheet and explain why they are deemed as errors.

LST Realty Private Limited Balance Sheet 1 Jan 2008 to 31 Dec 2008			
Assets		Liabilities	
Cash	\$9,500	Depreciation	\$2,560
Rental Expense	\$7,000	Salary Expense	\$9,780
Furniture	\$5,900	Accounts receivable	\$4,800
Accounts payable	\$5,900	Revenue	\$9,980
Equity	\$8,960		

(10 marks)

Question 3

- (a) Mr. Low is evaluating the purchase of a retail unit at a price of \$1,750,000. Based on the said asking price, expected future cash flows over a holding period of 6 years, and a discount rate of 8.5% per year, his calculations indicate a Net Present Value of +\$14,560. If the required rate of return is increased to 9.5% per annum, the Net Present Value is -\$7,680.
- (i) If he pays less than \$1,750,000 for the property, would the Internal Rate of Return be higher than 8.5% per annum? Why?  
(5 marks)
- (ii) If his required rate of return is 10% per year, is it advisable for him to buy the property for more than \$1,750,000? Why?  
(5 marks)
- (b) Information furnished by government agencies on the residential property market typically includes data on the median transaction price.

Define median transaction price and discuss its use for tracking residential price movements over time.

(10 marks)

Question 4

Write short notes on the following:

- (a) Evaluating Real Estate Investments via the DCF Approach.
- (b) Price Elasticity of Demand for Real Estate.
- (c) Valuation for Mortgage Purpose.
- (d) Functional Obsolescence.

(20 marks)

Question 5

- (a) Mr. Wong appointed Miss Chan as the sole-agent to sell his 24-year-old terrace house. He told her privately that he was selling the property because he could no longer tolerate his neighbours' late-night mahjong sessions. When a potential buyer by the name of Mr. Tan asked about the reason for the sale, Miss Chan replied that the seller was planning to relocate closer to his youngest son's home in Pasir Ris. The property was eventually sold to Mr. Tan.

Has Miss Chan breached any Code of Conduct and Ethics? Give reasons to support your answer.

(6 marks)

- (b) Consider the following advertisement of a firm: "We, the biggest team of real estate agents, are all ready to service your needs, be it buying your dream home or selling your current property. Our unbeatable record speaks for itself. Last year we handled the highest number of sales, much more than our nearest competitor."

Explain why this advertisement is deemed to have breached the Code of Conduct and Ethics.

(6 marks)

- (c) The direct comparison approach is invariably invoked for the valuation of HDB resale flats. Explain why it is the preferred method.

(8 marks)



Question 6

Mr. Chew is considering the purchase of a semi-detached bungalow as an investment. The asking price is \$2.35 million. The estimated unfurnished rent is \$5,500 per month. To finance the purchase of the property, he plans to take up a bank loan of \$1.5 million repayable over 20 years.

- (a) Enumerate and discuss the risks that Mr. Chew should consider when evaluating this proposed investment.

(10 marks)

- (b) "Since the initial yield of the proposed property investment is around 2.5% per year, it is not a prudent decision to go ahead with the investment. It is better to invest the funds in REITs which offer a better return." Should Mr. Chew heed this advice? Why?

(10 marks)

Question 7

- (a) Dr. Lam plans to start his dental practice in a shopping centre. A vacant 45-m<sup>2</sup> unit on the second storey is available on a 3-year lease at an asking rent of \$9,000 per month, exclusive of service charges. Another vacant 40-m<sup>2</sup> unit on the third storey is available for \$9,800 per month, exclusive of service charges.

His friend advises him to take up the unit on the second storey because it comes with a larger floor area but at a lower rent. Is this a good advice? Give reasons to support your view.

(10 marks)

- (b) Discuss how real estate agents could achieve a standard of professionalism that would meet public expectations.

(10 marks)

Question 8

Each part of this question carries two (2) marks. You are required to indicate the most appropriate answer for each part of this question in the answer script. No marks will be given if the answer is not clearly indicated. If more than one answer is given to any part, no marks will be awarded for that part.

- (I) Which one of the following statements is correct?
- (A) CPF savings cannot be used to finance the purchase of residential land for constructing a bungalow for owner occupation.
  - (B) In the direct comparison approach, one can use asking and offer prices to estimate the open market value of a property.
  - (C) "Stable monetary unit" is not one of the generally accepted accounting principles because credit facilities offered by a bank to the firm can be withdrawn at short notice.
  - (D) None of the above answers.

(II) Which one of the following statements is correct?

- (A) If regular and periodic maintenance has been carried out to an old property, it is reasonable to conclude that it will not be affected by economic obsolescence.
- (B) A property though built 20 years ago is not affected by functional obsolescence because there is an increasing preference for conserved properties.
- (C) The law of demand and supply does not apply to real estate markets because land is indestructible.
- (D) None of the above answers.

(III) Consider the following in relation to the supply of private housing: (i) high property prices; (ii) 10-year period between the peak and trough of a real estate cycle; (iii) long construction period of a project; (iv) elastic demand for private housing.

The inelasticity of supply in the short run is due to:

- (A) (i), (ii), (iii), and (iv).
- (B) (i) and (iii) only.
- (C) (iii) only.
- (D) (ii) and (iv) only.

(IV) Consider the following statements:

- (i) The principle of "Caveat Emptor" permits the seller's agent to release confidential information about why the vendor is selling the property.
- (ii) An agent can definitely be sued for negligence if a property is sold for less than its valuation.

- (A) Both statements are correct.
- (B) Both statements are incorrect.
- (C) Statement (i) is correct, but statement (ii) is incorrect.
- (D) Statement (ii) is correct, but statement (i) is incorrect.

(V) The payback period of a real estate investment is 5 years. The initial yield is 4%. Consider the following statements:

- (i) Based on the above information, we can definitely conclude that the Internal Rate of Return is 20%, being the reciprocal of the payback period.
- (ii) Based on the above information, we can definitely conclude that the Net Present Value of the investment will be positive if the required rate of return is 10%.

- (A) Statement (i) is correct while statement (ii) is incorrect.
- (B) Statement (ii) is correct while statement (i) is incorrect.
- (C) Both statements are correct.
- ☒ (D) Both statements are incorrect.

(VI) Which one of the following statements is correct?

- (A) An owner-occupied property will always fetch a price in excess of its open market value.
- (B) In evaluating the loan-to-value ratio of a residential property the bank will generally disregard the age of the applicant.
- (C) A schedule of commissions is prescribed by a professional body to ensure that firms will cover their costs plus a 50-percent profit margin.
- (D) None of the above answers.

(VII) Consider the following: (i) growth rate of the economy; (ii) growth rate of the number of retirees; and (iii) number of tourist arrivals. The demand for office space is likely to be influenced by

- (A) (i) only.
- (B) (ii) only.
- (C) (ii) and (iii) only.
- (D) (iii) only.

(VIII) Which one of the following statements is correct?

- (A) The objective of adopting cash-basis accounting is to ensure that a firm has sufficient cash to meet all its debt obligations. †
- (B) The profits method of valuation is often used to value retail properties whenever there is a lack of sales transactions.
- (C) The "going concern" concept ensures that revenue is recorded only when cash is received for services rendered by the firm.
- (D) A non-leveraged investment is not exposed to financial risk.

(IX) Consider the following statements:

- (i) The Net Present Value concept takes into consideration the time value of money.
- (ii) The Net Present Value concept considers only revenue receivable during the first 10 years of the investment.

- (A) Statement (i) is correct and statement (ii) is incorrect.
- (B) Statement (ii) is correct and statement (i) is incorrect.
- (C) Both statements are correct.
- (D) Both statements are incorrect.

(X) Consider the following features of real estate: (i) inelastic supply; (ii) immobility; (iii) indivisibility; and (iv) indestructibility.

The supply of mortgage loans is not affected by:

- (A) (i) only.
- (B) (i) and (iv) only.
- (C) (i), (ii), (iii), and (iv).
- (D) None of the above answers.

(20 marks)

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