

Rockwall CAD

Basics of

Appraising Property

For

Property Taxation

ROCKWALL CENTRAL APPRAISAL DISTRICT
841 Justin Rd.
Rockwall, Texas 75087

- c) Both the seller and purchaser seek to maximize their gains and neither is in a position to take advantage of the exigencies of the other.

Highest and Best Use

In order to determine the market value of property, the appraiser must determine the "highest and best" use of the property. The highest and best use is the use of the property that is its most profitable use at a specific time (as of January 1), that is legally permissible, physically possible and financially feasible. Highest and best use is not always the actual current use of the property. The only time highest and best use is not considered is in the appraisal of a residence homestead property. In this instance, the residence homestead value must be determined solely on the basis of its current use.

Data Collected

The appraisal district staff begins the appraisal process by performing data collection of all property. Staff appraisers will inspect each property noting the individual characteristics of the property that affect value such as size (square feet), age, quality of construction, physical condition, restrictions to use of property, terrain or topography, etc. The district has developed valuation schedules and models based on the different types of properties. Each property will be placed on the appropriate model based on its individual characteristics.

Statistical Analysis and Ratio Studies

Models are calibrated and adjusted annually through the use of ratio studies and statistical analysis. The district will compare actual sales prices of individual properties to the value produced to that property through the model and determine the appropriate adjustment that is needed for the model. Ratio studies allow the district to measure and evaluate the two major aspects of mass appraisal models:

Level of Appraisal Accuracy and Uniformity

- a) Level of appraisal accuracy refers to the overall ratio of appraised values to market values of properties within the same category or market area. Level measurements provide information about the degree to which mass appraisal models are working and what adjustments are warranted. The measures of appraisal level that are calculated are the median ratio, mean ratio and weighted mean ratio. These are also referred to as measures of central tendency.
- b) Level of appraisal uniformity refers to the degree to which properties are appraised at equal percentages of market value. Uniformity can be measured as
 - 1.) Coefficient of Dispersion (COD)
The COD is the most generally useful measure of variability. The COD measures the average percentage deviation of the ratios from the median ratio. The COD has the desirable feature that its interpretation does not depend on the assumption

for their differences from the subject. Finally, a market value for the subject is estimated from the adjusted sales prices of the comparable sales.

b) **Income Approach:**

This approach asks "What would an investor pay in anticipation of future income from the property?" The income approach is usually used to appraise types of properties that generate income, such as office buildings, hotels or retail centers. This approach is based on the principle that the value of an investment property reflects the quality and quantity of the income it is expected to generate over its life. That is, value is the estimated present value of future benefits (chiefly income and proceeds from the sale of the property).

Estimating the value of an income-producing property is done by capitalization. In its simplest form, capitalization is the division of a present income by an appropriate rate of return to estimate the value of the income stream.

In doing an income approach, the appraisal district will look at the market for typical rents and expenses of similar properties as it is the fee simple estate being appraised. The typical formula that will be used in the income approach is:

$$\begin{array}{r} \text{Potential Gross Rent} \\ \text{Less} \\ \text{Vacancy and Collection Loss} \\ \text{Plus} \\ \text{Miscellaneous Income} \\ \text{Equals} \\ \text{Effective Gross Rent} \\ \text{Less} \\ \text{Allowable Operating Expenses} \\ \text{Equals} \\ \text{Net Operating Income} \\ \text{Divided by} \\ \text{Capitalization Rate} \end{array}$$

c) **Cost Approach:**

This approach asks "How much would it cost to replace the property with one of equal utility?" The cost approach is justified in part by the principle of substitution; an informed buyer will pay no more for an improved property than the price of acquiring a vacant site and constructing a substitute building of equal utility, assuming no costly delays in construction. The cost approach requires estimates of land value, accrued depreciation and the current cost of constructing the improvements. Depreciation is subtracted from the current construction cost to obtain an estimate of improvement value.

Special-Purpose	1	2, 3	2, 3
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Land Valuation

In appraising land the appraiser will take into consideration the four basic factors that affect land values:

1. Physical Attributes of the Site- Ex. Topography
2. Economic Conditions- Ex. Location
3. Government Influences- Ex. Zoning
4. Social Standards- Ex. Country Club

There are four methods of appraising land used by our appraisers:

1. Sales Comparison (Market Approach)
This is the preferred method if sufficient sales data of vacant land is available. This method produces the most reliable indication of land value. In using this method the appraiser must make adjustments to the comparable sales for financing, time, locational characteristics, physical characteristics and any restrictions to the land.
2. Allocation by Ratio
This method works well for appraising lot values in a residential subdivision where few vacant lot sales are available. In this method the appraiser will:
 - Identify comparable sales of improved land
 - Estimate the ratio of land value to property value ratio
 - Apply the "typical" ratio to estimate the land value of the subject property
3. Allocation by Abstraction
In this method the appraiser will find the sale of a comparable improved property and subtract the depreciated replacement cost new of the improvement to arrive at the land value.
4. Capitalization of Ground Rent (Income Approach)
To capitalize a ground rent the appraiser must have reliable income information of rents of similar land and divide the market rent by the appropriate capitalization rate to produce an indication of value.

This handout was intended to give property owners the basic framework of property appraisals and does not include detailed information regarding property appraisal. For more information please feel free to contact our office at 972-771-2034 and one of our staff members will assist you with any questions you might have.