



2017-2018 MONTANA REAPPRAISAL PLAN

Montana Department of Revenue



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I. EXECUTIVE SUMMARY

The Montana Department of Revenue (department) is statutorily required to reappraise all taxable residential, commercial, industrial, and agricultural property every two years.

The Montana Constitution requires the department to equitably value all taxable property. This is accomplished by a mass appraisal performed in accordance with Montana law and industry standards and practices.

The 2017 Legislature will determine the tax rates for each property class based in part on the change of value in each class from the 2015-2016 reappraisal cycle.

Upon receipt of the department's updated values and the legislature's updated tax rates, the 1,400 taxing jurisdictions will set their budgets and determine the mill levies required to fund services provided in each taxing jurisdiction.

Each county treasurer will mail property tax bills in October/November 2017. The first half of the 2017 taxes will be due on November 30, 2017 and the second half due of the 2017 taxes on May 31, 2018.

II. INTRODUCTION

Montana law requires the department to adopt a comprehensive written reappraisal plan each reappraisal cycle. The reappraisal plan provides that all class three and class four property in each county is appraised at market value as of January 1, 2016, effective for the reappraisal cycle beginning on January 1, 2017 through December 31, 2018.

This document explains the department's general reappraisal plan, appraisal theory, mass appraisal process, data collection, valuation methodologies, measurements of reappraisal success, and a property owner's right to object to the department's value of their property.

III. GENERAL REAPPRAISAL PLAN

The 2017-2018 Montana Reappraisal Plan discusses in detail how the department accomplishes our statutory and constitutional requirements for the property owners of Montana.

A. Reappraisal Classes

1. *Class Three – Agricultural Property*

Class three is the largest use of land in the state of Montana as measured in the number of acres. The value of agricultural land is based on the productivity of the land. The five subclasses of agricultural land are: grazing land, tillable irrigated land, continuously cropped non-irrigated farm land, non-irrigated summer fallow farmland, and non-irrigated hayland.

2. *Class Four – Residential, Commercial, and Industrial Property*

Class four is the largest class of property in the state of Montana, as measured in both market value and the number of parcels. Class four property includes all residential, commercial and industrial land and improvements. Property in this class is valued at 100 percent of its market value.

B. Market Value Standard

Statutory law requires the department to appraise all taxable class three and class four property at 100 percent of its market value as of the valuation date. 15-7-111, MCA.

Market value is “the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of the relevant facts.” 15-8-111(1)-(2)(a), MCA.

C. Mass Appraisal Standard

The [Montana Constitution, Art. VIII](#), Sections 3 and 4 requires all taxable property to be uniformly reappraised. Statutory law requires all property to be reappraised as of a certain date. The valuation date for the 2017-2018 reappraisal cycle is January 1, 2016. The department reappraises property by conducting a mass appraisal in accordance with Standard 6 of the Uniform Standards of Appraisal Practice (USPAP). The department accomplishes this through the development of valuation models using statistical testing and standardized procedures.

D. Reappraisal Processes

1. *Identification of Market Areas*

All 56 counties in the state are separated into neighborhoods or market areas in accordance with market activity. See Exhibit A.

2. *Sales Verification and Trending Sales to Valuation Date*

Staff collects, verifies, and analyzes sales through the prior cycle to the valuation date of the current cycle. All sales are time trended to the valuation date of January 1, 2016, regardless of the sale date.

3. *Construction Costs Updated*

Staff collects construction cost data from local sources. If limited data is available locally, the department may utilize data from nationally accepted construction cost manuals such as Marshall & Swift, Richardson Engineering Services and RSMeans. The statewide construction costs represent average construction cost levels in the state. The statewide construction costs are adjusted using a local index and economic condition factors to reflect local market construction costs for locales throughout the state.

4. *Land Valuation Models*

Land models are built from the vacant land sales and reflect the market values of land in particular neighborhoods selling with similar characteristics, i.e., size, location, topography.

5. *Residential Market Models*

Market models are built using multiple regression analysis from the sales collected. After determining the primary property characteristics driving the property sale and the

weight those characteristics have on the property sale, comparable sales with characteristics similar to each subject property are used to value residential properties.

6. Commercial Income Models

Income models are built using income and expense data reported by commercial property owners and an analysis of the independent variables that affect gross income. These variables include, but are not limited to, types of property, and the quality, condition and location of the property.

7. Final Determination of Values

During the reappraisal process, appraisers consider each applicable approach to value for a given property. The appraiser then determines which of those methods results in a value that is most representative of the market value of the property. For residential property, the sales comparison approach to value and the cost approach to value are typically the most applicable methods. For commercial property, the income approach to value and the cost approach to value are typically the most applicable methods. For industrial property, the cost approach to value is typically the most applicable method due to the special use and uniqueness of the properties.

8. Classification and Appraisal Notices

In the first year of each reappraisal cycle, classification and appraisal notices are mailed to all property owners or purchasers under contract for deed. In the second year of each reappraisal cycle, Montana law states that the department shall mail to each property owner or purchaser under contract for deed a classification and appraisal notice only if there has been a change in ownership, classification, or valuation. The purpose of the classification and appraisal notice is to inform taxpayers of the market value and taxable value of their property for property tax purposes.

Taxpayers have 30 days from the date on the notice to dispute their property valuation or classification for the current tax year. Taxpayers have the right to file a Request for Informal Classification and Appraisal Review, (Form AB-26). Taxpayers also have the right to file a formal appeal with their local county tax appeal board in either year of the two-year reappraisal cycle, but may only do so once each appraisal cycle.

The Montana Legislature may mitigate the impact of the new reappraised values in the first year of the 2017-2018 cycle. However, the legislative session does not end until April 2017. Because the department is required to implement any legislative mitigation strategies that are adopted prior to mailing classification and appraisal notices, the department's mailing of classification and appraisal notices for tax year 2017 may be delayed.

County treasurers will mail the property tax bills by November 1, 2017. The first half of taxes will be due to the County Treasurer by November 30, 2017, and the second half are due May 31, 2018.

9. Informal Assessment Reviews and Appeals

Informal Assessment Reviews and Appeals will be discussed in Section XII.

10. Certification of Values

The department is responsible for annually certifying all taxable real and personal property to all taxing jurisdictions by the first Monday in August. 15-10-202, MCA

E. Valuation Sources

The 2017-2018 Montana Reappraisal Plan explains how the department values residential, commercial, and industrial real property. When valuing property using the cost approach to valuation, the department uses construction cost manuals such as Marshall & Swift, Richardson Engineering Services, or RSMeans, among others with a publication date as close to the valuation date as possible. When valuing agricultural land, the department uses productivity data from the US Department of Agriculture (USDA) Natural Resources Conservation Service (NRCS); and agricultural income and commodity prices from the USDA National Agricultural Statistics Service. Department staff routinely reference the 2017-2018 Montana Agricultural Land Classification Manual and the Appraisal Guide.

When valuing forest lands, the department will use forest costs provided by the State of Montana Department of Natural Resource and Conservation and stumpage values provided by Dr. David Jackson, University of Montana. The department will apply the forest costs and stumpage values to the 2015 forest lands reappraisal. The 2015 values will remain unchanged for the six-year cycle ending on December 31, 2020, unless a change in property characteristics impacts the value or a change in the property's classification.

F. Reappraisal Cycles

For the taxable years from January 1, 2017 through December 31, 2018, all class four residential, commercial, and industrial property will be appraised at market value as of January 1, 2016, in accordance with 15-7-111, MCA. Class three agricultural property will be appraised at the land's productive value as of January 1, 2016. Class ten forest land is appraised once every six years. The current reappraisal cycle for forest lands is 2015-2020. Class ten property was appraised as of January 1, 2014.

IV. APPRAISAL THEORY

This section explains the concepts of appraisal and how the department's appraisers utilize appraisal theory in determining a property's market value.

The International Association of Assessing Officers; IAAO, is the department's main resource for appraisal concepts, theory, policy development, and staff training courses. Specific textbooks utilized for this section included *Property Appraisal and Assessment Administration*, IAAO 1990. Gloudemans Robert, *Mass Appraisal of Real Property*, IAAO 1999. *Property Assessment Valuation*, Third Edition, IAAO 2010.

A. Rights and the Principals of Value

An appraisal is an educated opinion or estimate of value. It is the appraiser's responsibility to determine, through the appraisal process, the full market value of the property as of the valuation date.

B. Bundle of Rights

The terms "real estate" and "real property" are often used interchangeably. Generally speaking, real estate pertains to the land and the fixed improvements to the land such as structures and other appurtenances, whereas real property encompasses all the interests, benefits and rights enjoyed by the ownership of the real estate.

Real property ownership involves the bundle of rights that asserts the owner has the rights to enter it, use it, sell it, lease it, give it away, or refuse to do any of these as the owner so do chooses. These rights are guaranteed by law, but are subject to certain governmental and private restrictions.

The governmental restrictions are found in its power to:

- Tax property.
- Take property by condemnation for the benefit of the public, providing that just compensation is made to the owner (Eminent Domain).
- Police property by enforcing any regulations deemed necessary to promote the safety, health, morals and general welfare of the public.
- Provide for the reversion of ownership to the state in cases where a competent heir to the property cannot be ascertained (Escheat).

Private restrictions imposed upon property are often in the form of agreements incorporated into the deed. The deed also defines the total bundle of rights the buyer is acquiring.

Appraisals for ad valorem tax purposes generally assume the property is owned in fee simple, meaning that the total bundle of rights is considered to be intact.

C. The Nature and Meaning of Value

For ad valorem tax purposes, the value sought is market value. The descriptive term “market” indicates the activity of buyers and sellers. Market value is the price which an informed and intelligent buyer, fully aware of the existence of competing properties, and not being compelled to act, would pay for a particular property.

D. Value in Use vs. Value in Exchange

Value in use refers to the actual value of a commodity to a specific person, as opposed to value in exchange. Value in exchange generally refers to the dollar value of a commodity to buyers.

E. The Principle of Supply and Demand

Supply and demand are impacted by population growth, new techniques in transportation, purchasing power, price levels, wage rates, taxation, governmental controls, and scarcity. For example, a sudden population growth in an area will create an increase in demand for housing. If the demand increases at a higher rate than the supply, property values typically increase. As the supply is increased demand begins to taper off and property values typically decrease. Balance is reached when supply and demand are similar. When supply and demand are balanced, property values are typically stable.

F. The Principle of Highest and Best Use

The highest and best use for a property is the use that will produce the highest net return to the land for a given period of time within the limits of those uses which are legally permissible, physically possible, and economically feasible. In mass appraisal, the current highest and best use is usually considered to be the current use, that is, buildings will not be immediately demolished or replaced. However, this does not lessen the need to evaluate long-run highest and best use for different groups of property before reappraisal. The department is required to value based upon current use, known as value in use, due to statutory requirements.

G. The Principle of Change

The impact of change on the value of real property is demonstrated in the life cycle of a neighborhood. These cycles are characterized by three stages of evolution:

development and growth evidenced by improving values; leveling off evidenced by static values; and finally, decay evidenced by declining values.

H. The Principle of Substitution

Value is created by people in the market place. It is the function of translating demand into a commodity of exchange. When the benefits and advantages derived from two properties are equal, the lowest priced property receives the greatest demand. The informed buyer is not justified in paying anything more for a property than it would cost to acquire an equally desirable property. That is to say that the value of a property is established as that amount for which equally desirable comparable properties are being bought and sold in the market. This is the concept in determining property values and the basis of the valuation process.

V. MASS APPRAISAL PROCESS

Mass appraisal is different from a fee appraisal which looks at a single property on any given date. Mass appraisal is the systematic appraisal of groups of properties as of a given valuation date using standardized procedures and statistical testing. The valuation date for the 2017-2018 reappraisal cycle is January 1, 2016. The department adheres to the Uniform Standards of Mass Appraisal Practice (USPAP), Standard 6 when conducting its mass appraisal.

The department is required by law to fairly and equitably value all taxable property. The primary objective of mass appraisal is to equalize property values. In mass appraisal, the value of similar properties must be equalized together, in addition to being equalized within the market area. To accomplish this, the department's appraisers utilize the three approaches to value: the sales comparison approach, the cost approach, and the income approach. For residential property, the department primarily utilizes the sales comparison approach and the cost approach; for commercial property the department primarily utilizes the income approach and the cost approach and; for industrial property the cost approach is primarily utilized.

The International Association of Assessing Officers; IAAO, is the department's main resource for appraisal concepts, theory, policy development and staff training courses. Specific textbooks utilized for this section included *Property Appraisal and Assessment Administration*, IAAO 1990. Gloudemans Robert, *Mass Appraisal of Real Property*, IAAO 1999. *Property Assessment Valuation*, Third Edition, IAAO 2010.

A. Residential Property

The department's residential appraisers must rely heavily upon the sales comparison approach to value. The selling prices of comparable properties are analyzed using the same considerations as the buyers, such as, the location, size, quality, design, age, condition, desirability, and usefulness. For example, a prospective purchaser of a residential property is primarily interested in its capacity to render service to the family as a place to live. Its location, size, quality, design, age, condition, desirability and usefulness are the primary factors considered in making a selection. One property will eventually stand out to be more appealing than another. Thus, it is likewise the job of the department's appraisers to evaluate the relative degree of appeal of one property to another. The cost approach to value is also considered if a property is unique and cannot be grouped with other similar properties.

B. Commercial Property

The department requests income and expense information from owners of commercial property every two years. The data collected for individual properties is kept confidential and is aggregated for similar types of properties, i.e. apartments, retail businesses, etc. Income models are then developed to value the similar properties. The department also analyses sales to determine the capitalization rates by comparing the properties sales price and net operating income. Similar to the process the department uses to value residential property, the department's commercial appraisers analyze the considerations of prospective purchasers of commercial property. Purchasers of commercial property are primarily interested in the potential net return and tax shelter of the property. Commercial appraisers analyze the rental market and compare the income producing capabilities of one property to another. Since commercial property is generally not bought and sold as frequently as residential property, a reliable sales comparison approach cannot be easily established. Consequently, the department's appraisers rely heavily on the income approach.

C. Industrial Property

The prospective purchaser of industrial property is primarily interested in the overall utility value of the property. Of course, in evaluating the overall utility, individual consideration must be given to the land and each improvement on the land. Industrial buildings are generally of special purpose design that cannot readily be separated from the industrial operation for which they were built. As long as the operation remains effective, the building will hold its values; if the operation becomes obsolete, the building will also typically become obsolete. The upper limit of the building's value is its replacement cost new, and its present day usefulness in relation to the purpose for which it was originally designed.

Industrial appraisers will seldom be able to rely on the sales comparison approach because of the absence of comparable sales. It is also difficult to rely on the income approach because of the absence of comparable investments and the inability to accurately determine the contribution of each unit of production to the overall income produced. Appraisers must, therefore, rely heavily on the cost approach to value and determine the upper limit or replacement cost new of each improvement and the subsequent loss of value resulting overall from physical, functional, and economic factors.

D. Agricultural Property

The department uses a geographic information system (GIS), aerial imagery, and ownership data from the department's computer-assisted mass appraisal (CAMA) system to value agricultural land.

Department staff first classify the land into one of five land uses: non-irrigated summer fallow farmland; non-irrigated continuously cropped farmland; irrigated land; grazing land; or continuously cropped hay land. They use the most recent aerial photography, along with visiting the property if necessary for verification. A comparison between the old and new aerial imagery also assists appraisers in identifying any changes that occur. The imagery is provided by the National Agricultural Imagery Program (NAIP) which is administered by the Department of Agriculture Farm Service Agency (FSA) Aerial Photography Field Office in Salk Lake City. FSA has collected NAIP imagery in Montana every two years, since 2005.

Once classified, staff determine the productivity of the land based upon the soil type. The department receives soil productivity data from the USDA NRCS Soil Survey. The USDA NRCS soil survey is a digitized layer of data in our GIS technology that displays an estimate of each soil's productivity under its associated land use. This information is used to calculate the parcel's value.

The department takes into consideration average management practices and adjusts the NRCS data, if necessary to reflect those practices. For example, all counties receive an adjustment to the NRCS spring wheat productivity to reflect average management. The department may also make adjustments to productivity for special circumstances, such as, an area of high salinity resulting in a lower productivity than what the soil survey shows.

E. Equalization

Any effective approach to valuation must reflect buyers' motives in the market place. Motives influencing prospective buyers tend to differ depending upon the type of

property involved. For that reason, an appraiser's approach to value must differ accordingly. All the factors affecting value are analyzed and evaluated for each and every market area.

The fact that there are different approaches to value, some of which are more applicable to one type of property than to another, does not, by any means, preclude equalization between property types. The objective in each approach is to arrive at a price that an informed individual, fully aware of the existence of competing properties and not being compelled to act, is justified in paying for any one particular property. Underlying and fundamental to each of the approaches is the comparison process. Regardless of whether the principal criteria are actual selling prices, income producing capabilities, or functional usefulness, like properties are treated alike. The primary objective is equalization. The various approaches to value, although valid in themselves, are coordinated to produce values that are not only valid and accurate, but are also equitable. The same "yardstick" of value is applied to all properties utilizing systematic and uniform procedures.

Sales on all properties are not required to effectively apply the sales comparison approach. The same is true regarding any other approach. A comprehensive record of all the significant physical and economic characteristics of each property is required to compare the properties of "unknown" values with the properties of "known" values. All significant differences between properties must in some measure, either positively or negatively, be reflected in the final estimate of value.

This is a general explanation of the equalization process underlying the entire mass appraisal program. The program itself consists of various operational phases. Its success depends primarily upon the systematic coordination of collecting and recording data, analyzing the data, and processing the data to an indication of value.

VI. DATA COLLECTION

The collection and recordation of pertinent data is the foundation of the appraisal process. The data should include general supporting data, neighborhood data, and property specific data. General data is data necessary to develop the elements essential to the valuation process overall. Neighborhood data is those that relate to pre-delineated neighborhood units. Specific property data is the information compiled for each parcel of property. An appraiser will use general, neighborhood, and specific data to reach an estimate of value using the cost, sales comparison, and/or income approach to value.

The data must be comprehensive enough to allow an appraiser to adequately consider all factors that significantly affect property values. In keeping with the economics of a mass appraisal program, it is costly and impractical to collect, maintain, and process data of no or marginal contribution to the desired objectives.

Appraisers are primarily concerned with cost, and sales and income data, but they will also find it necessary to research and compile general socioeconomic information pertaining to the entire market area that may influence values. This information may assist an appraiser during the analytical phase of the process and should include, but is not limited to: population trends, prevailing geographical factors, primary transportation facilities, primary income sources, unemployment and income levels, institutional influences, the annual volume of new construction and ownership transfers, availability of vacant land, construction, labor and material costs, preponderance of residential rentals, and the amount of residential vacancies.

The department collects and maintains all property data in the CAMA system. The department provides this data to the public through a web application at property.mt.gov. In addition, the data from the CAMA system is electronically sent to the Montana Cadastral web application. Through both websites, property data may be accessed multiple ways, for example, by the property owner's name, address, geocode (property identifier), or assessment code. The data in both sites is updated nightly.

The International Association of Assessing Officers; IAAO, is the department's main resource for appraisal concepts, theory, policy development and staff training courses. Specific textbooks utilized for this section included *Property Appraisal and Assessment Administration*, IAAO 1990. Gloudemans Robert, *Mass Appraisal of Real Property*, IAAO 1999. *Property Assessment Valuation*, Third Edition, IAAO 2010.

A. Sales Data

1. *Sufficient Data Required*

The department's principle source for obtaining sales data in Montana is from Realty Transfer Certificates (RTCs). The law requires an RTC to be completed for any party transferring real property. The RTC is required regardless of whether the transfer is or is not evidenced by deed or instrument or any party presenting an instrument or deed evidencing a transfer of real estate for recordation. Real estate includes, among other things, land, growing timber, buildings, structures, fixtures, fences, and improvements to the land. The RTC must be filed with the county clerk and recorder at the time the instrument or deed evidencing a transfer of real estate is presented for recording. The department receives the RTC from the clerk and recorder's offices in every county in the state. If a transfer is by operation of law, the RTC and supporting documentation is filed

with the local Department of Revenue office in the county in which the property is located.

The department uses RTCs to collect parcel identification numbers, property classification codes, month and year of sale, selling prices, and to determine who filled out the form whether it is the buyer, seller, taxpayer agent, or title company. The department mails sales verification letters to buyer/seller to ensure accuracy of property characteristics and other information provided on the RTC. The law requires the department to utilize arms-length transactions in its valuation models. The department identifies arms-length transactions through RTCs, sales verification letters, and discussions with either buyers, sellers, or representative agents.

Sales data is used in each valuation method and therefore must be accurate and sufficient enough to: provide a representative sampling of comparable sales needed to apply the sales comparison approach; to derive unit land values and depreciation indicators needed to apply the cost approach; to derive gross rent multipliers and other elements of the capitalization rate needed to apply the income approach.

Other sources may include, multiple listing services, developers, realtors, lending institutions, and individual owners.

2. Determine Market Area and Neighborhoods

The department identifies neighborhoods based a high degree of homogeneity in residential amenities, land use, economic trends and housing characteristics such as structural quality, age, and condition. The neighborhood delineations are mapped and assigned a neighborhood identification code. The map and identification code uniquely identify each neighborhood.

Neighborhood data must be comprehensive enough to permit an appraiser to adequately consider all factors that influence value and to determine the variations in selling prices and income yields attributable to benefits arising from the location of one specific property as compared to another. The data should also include; the taxing district; the school district; the neighborhood identification code; special reasons for delineation (other than obvious physical and economic boundaries); the neighborhood characteristics such as the type (urban, suburban, etc.); trends (whether it is declining, improving, or relatively stable); accessibility to the central business district, shopping centers, interstate highways and primary transportation terminals; housing characteristics, (the estimated range of selling prices for residentially improved properties, and a rating of its relative durability).

3. Type of Data Collected

The data collected on each parcel in the department's CAMA system is: geocode or the parcel identification number, owner name, and mailing address, legal description, property address, property classification code, levy district, neighborhood code, site characteristics, and structural characteristics.

All the data is recorded on an electronic property record card (PRC) designed and formatted in such a way as to accommodate the listing of information and to facilitate data processing. In addition to the property data items noted above, space is provided on the property record card for a building sketch, land and building computations, summarizations, and memoranda. In keeping with the economy and efficiency of a mass appraisal program, the electronic card is formatted to minimize writing by including a sufficient amount of site and structural descriptive data that can be checked or identified in a drop down menu.

B. Cost Data

1. Sufficient Data Required

To apply the cost approach, cost data must be sufficient to develop or select and validate the pricing schedules and cost tables required to compute the replacement cost new of improvements.

2. Determine Market Area and Neighborhoods

The principal sources for obtaining cost data are builders and developers and in conjunction with new construction reviews.

3. Type of Data Collected

All data pertaining to the cost of total buildings in place should include the parcel identification number, property address, date of completion, construction costs, including all direct and indirect costs, name of builder, source of information, structural characteristics, and other information pertinent to analysis.

C. Income and Expense Data

1. Sufficient Data Required

Income and expense data is sufficient enough to derive capitalization rates and accurate estimates of net income needed to apply the income approach.

Income and expense data includes both general data regarding existing financial attitudes and practices, and specific data regarding the actual incomes and expenses realized by specific properties.

2. Sources of Data Collected

The principal sources for obtaining the general financial data are investors, lending institutions, and property managers. The primary sources for obtaining specific data are the individual property owners and/or tenants.

3. Type of Data Collected

General data includes: equity return expectations, gross rentals, vacancy and operating cost expectations and trends, prevailing property management costs, and prevailing mortgage costs. The general data is documented in conjunction with the development of capitalization procedural guidelines.

Specific data includes: the identification number, property address or building ID, information sources, the amount of equity, the mortgage and lease terms, and an itemized account of the annual gross income, vacancy loss, and operating expenses for the most recent two year period. The specific data, since it is often considered confidential and not subject to public access, is recorded on special forms, designed in such a way as to accommodate the property owner or designated agent in submitting the required information.

D. Data Processing

This is an analysis of the data inventoried and the processing of the data to an indication of value through the use of the cost, sales comparison, and income approaches.

It is necessary to analyze cost, sales comparison, and income data in order to provide a basis for validating the appropriate cost schedule and tables required to compute the replacement cost new of all buildings and structures; for establishing comparative unit land values for each type of property; for establishing the appropriate depreciation tables and guidelines for each type of property; and for developing gross rent multipliers, economic rent and operating expense norms, capitalization rate tables and other related standards and norms required to effect the mass appraisal of all the property within an entire market area on an equitable basis.

After establishing the appropriate standards and norms, the specific data compiled for each property is analyzed. This is done by giving due consideration to the factors influencing the value of that particular property as compared to another, and then to process the data into an indication of value.

Any one, or all three of the approaches, if applied properly, lead to an indication of market value; of primary concern is applying the approaches on an equitable basis. This includes the following activities:

- Verifying the accuracy of each of the characteristics recorded on the data collection card;
- Determining the proper quality grade and design factor to be applied to each building to account for variations from the base specifications;
- Making a judgment of the overall condition, desirability, and usefulness of each improvement in order to arrive at a sound allowance for depreciation;
- Capitalization of net income capabilities into an indication of value in order to determine the loss of value attributable to functional and economic obsolescence;
- Adding the depreciated value of all improvements to the land value, and reviewing the total property value in relation to the value of comparable properties; and
- Determining that the total property value established can be correlated to actual sales of comparable properties.

No mass appraisal program, regardless of how skillfully administered, can ever be expected to be error free. The department's mass appraisal must be fine-tuned and this can best be done by giving the taxpayer an opportunity to question the value placed upon his property and to produce evidence that the value is inaccurate or inequitable. Refer to Section XII for more information explaining how property owners can object to the department's appraised market value.

E. Property Reviews

Department staff conduct individual property inspections, building permit reviews, sales data verification reviews, and electronic data reviews on 1/6th of the total properties each year for three two-year cycles. The department encourages property owners to verify the accuracy of their property record on either the department's web application at property.mt.gov or the Montana Cadastral web application or by visiting our local revenue office in which the property is located.

VII. VALUATION METHODS

The department determines the best approach to value based upon the type of property and the quantity and quality of information available. Not all approaches are relevant nor are they necessarily pertinent in every valuation, even though the department reviews and considers each of the following approaches to value: sales comparison, cost, and income approach.

The International Association of Assessing Officers; IAAO, is the main resource for appraisal concepts, theory, policy development and staff training courses. Specific

textbooks utilized for this section included *Property Appraisal and Assessment Administration*, IAAO 1990. Gloudemans Robert, *Mass Appraisal of Real Property*, IAAO 1999. *Property Assessment Valuation*, Third Edition, IAAO 2010.

A. Sales Comparison Approach

An indication of the value of a property can be derived by analyzing the selling prices of comparable properties. The use of this technique involves the selection of a sufficient number of valid comparable sales and the adjustment of each sale to the subject property to account for variations in time, location, site and structural characteristics.

The appraiser selects comparable and valid market transactions, and weighs the sales by giving consideration to all factors significant to value and adjusting each to the subject property. The comparable sites must be used in the same way as is the subject property, and subjected to the same governmental restrictions. It is also preferable, whenever possible, to select comparable sales from the same or similar neighborhood. The primary adjustments account for variations in time, location, and physical characteristics to include size, as well as other factors which may significantly influence the selling price and extracted from the market; such as, quality of the improvements, number of bedrooms, bathrooms, style, and story height.

During the process of adjusting the comparable sales to account for variations between the sales and the subject property, the appraiser must exercise great care to include all significant factors and to properly consider the impact of each of the factors upon the total value.

1. *Selecting Valid Comparable Sales*

Since market value is defined in 15-8-111, MCA as “the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts,” it follows that if market value is to be derived from analyzing comparable sales, that the sales must represent valid “arm’s length” transactions. Due consideration is given to the conditions and circumstances of each sale before selecting the sales for analysis. Some examples of sales which may not reflect valid market conditions are as follows:

- Sales in connection with foreclosures, bankruptcies, condemnations and other legal action.
- Sales to or by federal, state, county and local governmental agencies.
- Sales to or by religious, charitable or benevolent tax exempt agencies.
- Sales involving family transfers.
- Sales involving intra-corporate affiliations.
- Sales involving the retention of life interests.
- Sales involving cemetery lots.
- Sales involving mineral or timber rights, and access or drainage rights
- Sales involving the transfer of part interests.

In addition to selecting valid market transactions, it is equally important to select properties which are truly comparable to the property being appraised.

The comparable and subject properties must exhibit the same use, and the site and structural characteristics must exhibit an acceptable degree of comparability.

2. Processing Comparable Sales

All comparable sales must be adjusted to the subject property to account for variations in time and location. The other major elements of comparison will differ depending upon the type of property being appraised. In selecting these elements, the appraiser must give prime consideration to the same factors that influence the prospective buyers of particular types of properties.

a. Residential Property

The typical home buyer is interested in the property's capacity to provide the family with a place to live. Primary concerns include the living area, utility area, number of rooms, number of baths, age, structural quality and condition, the presence of a modern kitchen and recreational conveniences of the house. Equally important is the location and neighborhood, including the proximity to quality of schools, public transportation and recreational and shopping facilities.

b. Commercial Property

The typical buyer of commercial property, including warehouses and certain light industrial plants, is primarily concerned with its capability to produce revenue. Of special interest will be the age, design and structural quality and condition of the improvements, the parking facilities, and the location relative to transportation, labor markets and trade centers.

In applying the sales comparison approach to commercial/industrial property, the appraiser will generally find it difficult to locate a sufficient number of comparable sales,

especially for properties which are truly comparable in their entirety. It will, therefore, be necessary to select smaller units of comparison such as price per square foot, per unit, per room, etc. In doing so, great care must be exercised in selecting a unit of comparison that represents a logical common denominator for the properties being compared. Using such units of comparison enables the appraiser to compare two properties which are similar in use and structural features, but different significantly in size and other characteristics.

c. Adjusting Comparable Sales to Subject Property

After the appraiser has selected the major factors of comparison, the appraiser must adjust each of the factors to the subject property. When comparing the site, adjustments for size, location, accessibility, and site improvements must be made. When comparing the structures, adjustments for size, quality, design, condition, and significant structural and mechanical components also must be made. The adjusted selling prices of the comparable properties will establish a range in value in which the value of the subject property will fall. Further analysis of the factors should enable the appraiser to narrow the range of the value that is most applicable to the subject property.

3. Land Valuation

In making appraisals for ad valorem tax purposes, it is generally necessary to estimate separate values for the land and the improvements on the land. In actuality, the two are not separated and the final estimate of the property as a single unit must be given prime consideration. There are a number of reasons why the department must estimate separate values for the land and the improvements when implementing the mass appraisal program:

- An estimate of land value is required in the application of the cost approach.
- An estimate of land value is required to be deducted from the total property selling price in order to derive indications of depreciation through market data analysis. Depreciation is equal to the difference between the replacement cost new of a structure and the actual price paid in the market place for the structure.
- Land is not a depreciable item, therefore, a separate estimate of land value is required for bookkeeping and accounting purposes; likewise, the total capitalization rate applicable to land may differ from the rate applicable to the improvements on the land.
- Since land may or may not be used to its highest potential, the value of land may be completely independent of the existing improvements on the land.

- Applications of the sales comparison approach are the primary techniques used in land valuation. When sufficient sales data are not available, the appraiser resorts to other methods. In any case, land values must reflect market value in each neighborhood or market area, they should also account adequately for differences in size, topography, and so forth among individual parcels.
- The utility of a site will vary due to the frontage, width, depth, and overall area. Similarly, unit land values should be adjusted to account for differences in size between the comparable and the subject property. Since such an adjustment is generally necessary for each lot, it is beneficial that the appraiser adopts and/or develops standardized procedures for adjusting the lot size and the unit values to account for the variation. It is not uncommon for all lots within a development to market at the same price. Should data indicate this, it is necessary to make alterations or adjustments to maintain this value level. In some cases, a “site value” concept has an advantage. Some of the techniques commonly employed are:
 - Standard lot sizing techniques which provide for the adjustment of the frontage, width, and depth of irregular shaped lots to make the units of measurement more comparable with uniform rectangular lots;
 - Standard Depth Tables provide for the adjustment of front foot unit values to account for variations in depth from a predetermined norm;
 - Frontage Tables provide for the adjustment of front footage unit values to account for variations in the relative utility value of excessive or insufficient frontage as compared to a predetermined norm; and
 - Acreage or Square Footage Tables provide for the adjustment of unit values to account for variations in the relative utility value of excessive or insufficient land sizes as compared to a predetermined norm.

a. Abstraction Method

While it is preferable to use sales of unimproved lots for comparables, it is not always possible to do so. Older neighborhoods are not likely to yield a sufficient number of representative sales of unimproved lots to permit a valid analysis. In such cases, it is necessary to consider improved property sales and to estimate the portion of the selling price applicable to the structure. The procedure is to:

- 1.) estimate the replacement cost of the buildings as of the date of sale;
- 2.) estimate the accrued depreciation and deduct that amount from the replacement cost; and
- 3.) deduct the resulting estimated selling price of the buildings from the total selling price of the property to derive the portion of the selling price which can be allocated to the land.

In the abstraction method, improvement values obtained from a cost estimation model are subtracted from the sales prices of improved parcels to yield residual land value estimates:

Sales price (SP) minus improvement value (IV) equals land value (LV); or

$$SP - IV = LV$$

These calculated values are then used as a supplement or as an alternative to vacant land sales in application of the sales comparison approach. The method is particularly useful in highly developed areas where there are few, if any, vacant land sales. Its reliability depends on the accuracy of the sales data and improvement values used in the analysis. In general, the method is more accurate for parcels with relatively new structures, for which replacement cost and depreciation are more easily estimated, or in high demand areas where the land value supersedes the improvement value.

b. *Allocation*

One technique that may be used to establish a broad indication of land values is a “typical” allocation or ratio method. In this technique, the ratio of the land value to the total value of improved properties is observed in situations where there is good market and/or cost evidence to support both the land values and total values.

This market-abstracted ratio is then applied to similar properties where the total values are known, but the allocation of values between land and improvements are not known. The ratio is usually expressed as a percentage which represents the portion of the total improved value that is land value, or as a formula:

$$\frac{V1}{V2} \times 100\% = V3$$

Where:

V1 = Total Land Value

V2 = Total Property Value

V3 = Percent Land is of Total Property Value

This technique can be used on most types of improved properties, with important exceptions being farms and recreational facilities, provided that the necessary sales comparison and/or cost information is available. In actual practice, available sales comparison information limits this technique primarily to residential properties, and to a much lesser extent, commercial and industrial properties such as apartments, offices, shopping centers, and warehouses.

The ratio technique cannot give exact indications of land values. It is still useful, however, when used in conjunction with other techniques of estimating land values because it provides an indication of the reasonableness of the final estimate of land value.

The ratio is extracted from available market information and applied to closely similar properties. Any factor that affects values may also affect the ratio of values. Zoning is particularly important because it may require more or fewer improvements to be made to the land, or may require a larger or smaller minimum size. This tends to have a bearing on the land values, and so it may also influence the ratio of values considerably from community to community.

The following is an example of a residential land valuation:

1.) Market information derived from an active new subdivision:

Typical Lot Sale Price (most lots equivalent) \$15,000
Improved Lot Sales (range)
 \$65,000 to \$75,000
 \$15,000/\$65,000=23%
 \$15,000/\$75,000=20%
Indicated ratio: 20%-23%

2.) Similar subdivision, but 100% developed:

Improved Lot Sales (range)
 \$85,000 to \$105,000

Broadest Indicated Range of Lot Values

 \$85,000 x 20% = \$17,000
 \$105,000 x 23% = \$24,150
Value Range: \$17,000 to \$24,150

Narrowest Indicated Range of Lot Values

$\$85,000 \times 23\% = \$19,550$

$\$105,000 \times 20\% = \$21,000$

Value Range: \$19,550 to \$21,000

If both lots and improvements vary considerably, the broadest range is most appropriate. If most lots vary little and are judged equivalent but the improvements vary somewhat, the narrowest range is appropriate. Most subdivisions exhibit a combination of the two ranges, showing a narrow typical range, but a wider actual range of land values.

c. *Land Residual*

In the absence of sufficient market data, income-producing land may be valued by determining the portion of the net income attributable to the land and capitalizing the net income into an indication of value. This technique is rarely used by the department but is still considered a viable alternative method for land valuation.

B. Cost Approach

The cost approach involves making an estimate of the depreciated cost of reproducing or replacing the building and site improvements. Reproduction cost refers to the cost at a given point in time of reproducing a replica property, whereas replacement cost refers to the cost of producing improvements of equal utility.

Depreciation is deducted from replacement or reproduction cost new to account for losses in value caused by physical deterioration, functional obsolescence, and external or economic obsolescence. The depreciated cost is then added to the estimated value of the land to determine an indication of value.

The significance of the cost approach lies in the extent of its application. It is the one approach that can be used on all types of construction. It is a starting point for appraisers, and therefore, it is a very effective yardstick in any equalization program for ad valorem taxes. Its widest application is in the appraisal of properties where the lack of adequate market and income data preclude the reasonable application of the other traditional approaches.

1. *Applying the Cost Approach*

Estimating the value of the land and adding the land value to the depreciated cost of the structures will result in a valid indication of value. The formula is *estimated land value + estimated replacement cost new of structures - estimated depreciation = an indication of property value.*

Since estimating the land value is covered in a separate section, this section will cover replacement cost and depreciation.

2. Replacement Cost

Replacement cost is the current cost of producing building and/or other site improvement of equal utility to the subject property; it may or may not be the cost of reproducing a replica property. It is not to be confused with reproduction cost, which refers to a substitute replica property. In a particular situation the two concepts may be interchangeable, but they are not necessarily so. They both, however, have application in the cost approach to value, the difference being reconciled in the consideration of depreciation allowances.

In actual practice, outside of a few historic type communities, developers and builders, for obvious economic reasons, replace buildings rather than reproduce them.

It logically follows that if an appraiser's job is to measure the actions of knowledgeable persons in the market place, the use of proper replacement costs should provide an accurate starting point in the valuation of most improvements.

The replacement cost includes the total cost of construction incurred by the builder whether preliminary to, during the course of, or after completion of the construction of a particular building. Among these costs are material, labor, all subcontracts, builders' overhead and profit, architectural and engineering fees, consultation fees, survey and permit fees, legal fees, taxes, insurance, and the cost of interim financing.

3. Estimating Replacement Cost

The department may estimate replacement costs by using four methods: quantity survey method, unit-in-place or segregated method, comparative or square foot method, and trended original cost method.

a. Quantity Survey Method

The quantity survey method involves a detailed itemized estimate of the quantities of various materials used, labor and equipment requirements, architect and engineering fees, contractor's overhead and profit, and other related costs. Contractors and cost estimators primarily use this method for bidding and budgetary purposes and is much too labor intensive and costly to be effective in every day appraisal work, especially in the mass appraisal field. However, the quantity survey method, can be useful in developing certain unit-in-place costs which can be more readily applied to estimating costs for appraisal purposes.

b. *Unit-in-place Method*

The unit-in-place method or segregated cost method, is employed by combining direct and indirect costs, including material, labor, overhead and profit, into a single unit-in-place. When the unit in place is multiplied by the area of the portion of the building being priced, it results in a total cost estimate for various structural components. The prices established for the specified components are related to their most common units of measurement such as cost per yard, cost per lineal foot, and cost per square foot.

The unit prices can then be multiplied by the respective quantities found in the composition of the subject building to derive the whole dollar component cost, the sum of which is equal to the estimated cost of the entire building, providing of course, that due consideration is given to all other indirect costs, which may be applicable.

c. *Comparative Unit or Square Foot Method*

The comparative unit or square foot method is the easiest, fastest, and most widely used method of cost estimation. Both direct and indirect costs, along with entrepreneurial profit, are summed and divided by an appropriate unit such as square feet area or cubic feet of volume, to derive a cost per unit. Comparative costs can be obtained from nationally published cost manuals or developed locally from an analysis of actual costs of benchmark structures. These costs are arranged in schedules based on type and quality of construction, size, and shape.

Percentage or lump sum adjustments for features not included in the comparative unit cost can be made with the unit-in-place method.

d. *Trended Original Cost Method*

The trended original cost method obtains an estimate of the reproduction cost of a structure by trending its historical cost with a factor from an appropriate construction cost index. The trended original cost method can be used to estimate current costs of structures for which comparable cost data are not readily available. It is especially useful for updating the cost estimate of recently constructed properties.

Developed and applied properly, these pricing techniques will assist the appraiser in arriving at valid and accurate estimates of replacement cost new as of a given time. That cost generally represents the upper limit of value of a structure. The difference between its replacement cost new and its present value is depreciation. The final step in completing the cost approach then is to estimate the amount of depreciation and deduct it from the replacement cost new.

4. Depreciation

Depreciation can be defined as a loss in value from all causes. As applied to real estate, it represents the loss in value between market value and the sum of the replacement cost new of the improvements plus the land value as of a given time. The causes for the loss in value may be divided into three broad classifications: physical deterioration, functional obsolescence, and economic obsolescence.

a. Physical Deterioration

Physical deterioration involves the wearing out of the various building components, and refers to both short life and long life terms, through the action of the elements, age, and use. The condition may be considered either curable or incurable, depending upon whether it is practical and economically feasible to cure the deficiency by repair and replacement.

b. Functional Obsolescence

Functional obsolescence is a condition caused either by inadequacies or over adequacies in design, style, composition, or arrangement inherent to the structure itself, which tend to lessen its usefulness.

Total accrued depreciation may be derived by first estimating the total useful life of a structure and then translating its present condition, desirability, and usefulness into an effective age rather than an actual age. This represents the percentage of the property's total life which has been used up. The effective age is then subtracted from the base year to arrive at the effective year.

Like physical deterioration, functional obsolescence may be considered either curable or incurable. Some of the more common examples of functional obsolescence are excessive wall and ceiling heights, excessive structural construction, surplus capacity, ineffective layouts, and inadequate building services.

c. Economic Obsolescence

Economic obsolescence, also referred to as external obsolescence, is a condition caused by factors extraneous to the property itself, such as changes in population characteristics and economic trends, encroachment of inharmonious land uses, excessive taxes, and governmental restrictions. The condition is generally incurable in that the cause or causes lie outside the property owner's control.

5. Estimating Depreciation

An estimate of depreciation represents an opinion of the appraiser as to the degree that the present and future appeal of a property has been diminished by physical deterioration, functional obsolescence, or economic obsolescence. Of the three

estimates necessary to the cost approach, it is the one most difficult to make. The accuracy of the estimate will be a product of the appraiser's experience in recognizing the symptoms of deterioration and obsolescence and the ability to exercise sound judgment in equating all observations to the proper monetary allowance to be deducted from the replacement cost new. There are several acceptable methods which may be employed:

- Physical deterioration and/or functional obsolescence can be measured by observing and comparing the physical condition and/or functional deficiencies of the subject property as of a given time with either an actual or hypothetical, comparable, new and properly planned structure.
- Curable physical deterioration and functional obsolescence can be measured by estimating the cost of restoring each item of depreciation to a physical condition as good as new, estimating the cost of eliminating the functional deficiency.
- Functional and economic obsolescence can be measured by capitalizing the estimated loss in rent due to the structural deficiency or lack of market demand.
- Total accrued depreciation may also be estimated by deriving the amount of depreciation recognized by the purchase price of the property. The loss of value is the difference between the cost of replacing the structure new and its actual selling price which is equal to the total property selling price less the estimated value of the land.

C. Income Approach

The income approach defines value as the present worth of future benefits of the property by the capitalization of the net income stream over the remaining economic life of the property. This approach involves making an estimate of the effective gross income of a property. The department's appraisers derive this estimate by deducting the appropriate vacancy and collection losses from its estimated economic rent, as shown by the yield of comparable properties. From this figure, applicable operating expenses are deducted, resulting in an estimate of net income which may then be capitalized into an indication of value. The basic formula is: value equals net income divided by capitalization rate.

1. *The Principals of Capitalization*

Capitalization is the process for converting the net income produced by property into an indication of value.

The most prominent methods of capitalization are direct capitalization, utilizing the direct comparison method of rate selection, straight-line capitalization, sinking fund

capitalization, and annuity capitalization. Each of these is a valid method for capitalizing income into an indication of value. The basis for their validity lies in the action of the market, which indicates that the value of income producing property can be derived by equating the net income with the net return anticipated by informed investors. This can be expressed in terms of a simple equation:

$$\text{capitalization rate} = \frac{\text{Net Income}}{\text{Sale Price}}$$

2. Direct Capitalization

The department uses the direct capitalization method. The appraiser determines a single “overall” capitalization rate. This is calculated by analyzing actual market sales of similar types of properties. The appraiser develops the net income of each property, and divides the net income by the sales price to arrive at an overall rate to provide an indication of value.

3. Exploring the Rental Market

The starting point for an appraiser is an investigation of current economic rent in a specific area in order to establish a sound basis for estimating the gross income that should be returned from competitive properties. The appraiser makes a distinction between economic rent, and the rent which property is normally expected to produce on the open market, as opposed to control rent or the rent which a property is actually realizing at the time of the appraisal due to lease terms established sometime in the past.

The first step is to obtain specific income and expense data (I&E) on properties which best typify normal market activity. The data is necessary to develop local guidelines for establishing the economic rent and related expenses for various types of properties.

The next step is to similarly collect income and expense data on individual properties, and to evaluate the data against the established guidelines.

The collection of I&E data is an essential phase in the valuation of commercial properties. The appraiser is primarily concerned with the potential earning power of the property. The objective is to estimate its expected net income. I&E statements of past years are valuable only to the extent which they serve this end. The appraiser should consider the following factors when evaluating I&E data in order to arrive at an accurate and realistic estimate of net income.

4. Income Data Analysis

The analysis of income data collected requires us to ask the following questions:

- Was the reported income produced entirely by the subject property? Very often the rental will include an amount attributable to one or more additional parcels of real estate. In this case, it would be necessary to obtain the proper allocations of rent.
- Was the income attributable to the subject property as it physically existed at the time of the appraisal, or did the appraisal include the value of leasehold improvements and remodeling for which the tenant paid in addition to rent? If so, it may be necessary to adjust the income to reflect economic rent.
- Does the reported income represent a full year's return? It is often advisable to obtain both monthly and annual amounts as a cross check.
- Does the income reflect current economic rent? Is part or all of the income predicated on old leases? If so, what are the provisions for renewal options and rates?
- Does the reported income reflect 100% occupancy? What percentage of occupancy does it reflect? Is this percentage typical of this type of property, or is it due to special nonrecurring causes?
- Does the income include rental for all marketable space? Does it include an allowance for space, if any, which is either owner or manager occupied? Is the allowance realistic?
- Is the income attributable directly to the real estate and conventional amenities? Is some of the income derived from furnishings and appliances? If so, it will be necessary to adjust the income or make provisions for reserves to eventually replace them, whichever local custom dictates.

In many properties, an actual rental does not exist because the real estate is owner occupied. In this event it is necessary to obtain other information to provide a basis to estimate economic rent. The information required pertains to the business operation using the property. Proper analysis of the annual operating statements, including gross sales or receipts, can provide an accurate estimate of economic rent.

Information requirements for a few of the more common property uses are as follows:

Retail Stores: The annual net gross sales which is equal to the gross sales less returned merchandise;

Hotels and Motels: The annual operating statement. If retail or office space is leased in these properties, obtain the actual rent paid.

Theaters: The annual gross receipts including admission and concessions and seating capacity.

Automobile Parking: The annual gross receipts.

5. *Expense Data Analysis*

An appraiser considers only those expenses which are applicable to the cost of ownership; that is, those expenses which are normally owner incurred. Any portion of the expenses incurred directly or indirectly by the tenant are not considered. Each expense item must be both legitimate and accurate. They must be consistent with the established guidelines and norms and with the expenses incurred by comparable properties.

a. *Management Costs*

Management costs refer to the cost of administration. These charges realistically reflect what a real estate management company would actually charge to manage the property. If no management fee is shown on the statement, the appraiser makes an allowance. On the other hand, if excessive management charges are reported the appraiser will disregard the reported charges and uses an amount which he/she deems appropriate and consistent with comparable type properties. The cost of management bears a relationship with the risk of ownership and will generally range between four percent to ten percent of the gross income.

b. *General Expenses*

General expenses may include such items as the cost of services and supplies not charged to a particular category. Unemployment and F.I.C.A. taxes, worker's compensation, and other employee insurance plans are usually legitimate deductions when employees are a part of the building operation.

c. *Reimbursed Expenses*

Reimbursed expenses refer to the expenses associated with the maintenance of public or common areas of a commercial property. This expense is passed on to the tenants and should only be considered when the amount of reimbursement is included as income.

d. *Miscellaneous Expenses*

Miscellaneous expenses are the catch all category for incidentals. Miscellaneous expenses should reflect a very nominal percentage of the income. If expenses reported seem to be excessive, the appraiser must examine the figures carefully in order to determine if they are legitimate expenses and if so, to allocate them to their proper category.

e. *Cleaning Expenses*

Cleaning expenses are legitimate charges. They can be for such items as general housekeeping and maid service, and include the total cost of labor and related supplies. All or a portion of the cleaning services may be provided by outside firms working on a

“contract” basis. Cleaning expenses vary considerably and are particularly significant in operations such as offices and hotels. Rule of thumb norms for various operations are made available through national management associations. The appraiser will generally have little difficulty in establishing local guidelines.

f. *Utility Expenses*

Utilities are generally legitimate expenses and if reported accurately, need very little reconstruction by the appraiser other than to determine if the charges are consistent with comparable properties.

Heat and Air Conditioning costs are often reported separately and in addition to utilities. The expenses include the cost of fuel other than the above mentioned utilities, and may include, especially in large installations, the cost of related supplies, inspection fees, and maintenance charges.

g. *Elevator Expenses*

Elevator expenses, including the cost of repairs and services, are legitimate deductions, and are generally handled through service contracts. These fees can generally be regarded as fairly stable annual recurring expenses.

h. *Repairs and Maintenance Expenses*

Repairs and maintenance expenses reported for any given year may not necessarily be a true indication of the average or typical annual expense for these items. For example, a statement could reflect a substantial expenditure for a specific year, possibly because the roof was replaced and/or several items of deferred maintenance were corrected, and yet the statement for the following year may indicate that repairs and maintenance charges were practically nonexistent. An appraiser should obtain complete economic history on each property in order to make a proper judgment as to the average annual expense for these items, or include a proper allowance based on norms for the type and age of the improvements to cover annual expense. Since it is neither possible nor practical to obtain enough economic history on every property, the amounts reported for repairs and maintenance are estimated by the appraiser.

i. *Insurance Expenses*

Fire extended coverage and owner’s liability are the main insurance expense items.

j. *Real Estate Taxes*

In making appraisals for tax purposes, the appraiser must exclude the actual amount reported for real estate taxes. Since future taxes will be based on the appraised value, the appraiser must express the taxes as a factor of the estimated value. This can be

done by including an additional percentage in the capitalization rate to account for real estate taxes.

k. *Depreciation*

The figure shown for depreciation on an operating statement is a bookkeeping figure which the owner uses for Internal Revenue Service purposes and is not considered in the income approach.

l. *Interest Expense*

Although interest is considered a legitimate expense, it is always included in the capitalization rate. Most property is appraised as if it were free and clear; however, the appraiser does consider the interest of a current mortgage in the capitalization rate build-up.

m. *Land Rent*

When appraising for real estate tax purposes, only the sum of the leasehold and the leased fee is usually considered. Land rent is not deducted as an expense. Considered separately, rent from a ground lease would be an expense to the leasehold interest and an income to the leased fee. However, if land were rented from another property to supply additional parking for example, that land rent would be an allowable expense.

It is obvious that there are some expense items encountered on operating statements that appraisers should not consider as allowable. This is because they are interested in legitimate cash expenses only. Income statements are usually designed for income tax purposes where credit can be taken for borrowing costs and theoretical depreciation losses.

It is virtually impossible and certainly not always practical to obtain a complete economic history on every commercial property being appraised. On many properties, however, detailed economic information can be obtained through the use of income and expense forms. One must realistically recognize the fact that the data obtainable on some properties is definitely limited.

In most cases, the gross income and a list of the services and amenities furnished can be obtained during the data gathering operation. However, in order to ensure a sound appraisal, it may be necessary to estimate the fixed and operating expenses. This is best accomplished by setting guidelines for expenses, based on a percent of effective gross income or a cost per square foot of leasable area. These percentages or costs will vary depending on the services supplied and the type of property.

VIII. PLANNING AND ORGANIZATION

The department conducts a number of processes on an annual basis in preparation for our annual certification of values to the counties. The department also conducts a number of activities in preparation for the subsequent reappraisal cycle. See Exhibit B for a chart outlining our primary activities for both our annual and reappraisal work.

IX. PROPERTY ASSESSMENT DIVISION RESOURCES

The Property Assessment Division of the Department of Revenue (PAD/DOR) is comprised of a central office located in Helena, four regional areas, and 56 local revenue offices, one in each county seat. PAD/DOR conducts its work by employing managers, appraisers, and property valuation specialists in our local county offices and managers and management analysts in our central office.

The central office staff provides: technical assistance to the field offices; maintains the CAMA system; manages cadastral data; and works closely with the local revenue offices in collecting data, conducting quality assurance, and analyzing the data. Data collection and data management are key components to accurate appraisals. The field offices provide: customer service directly to the property taxpayer; collect data; perform quality assurance; analyze data; and work closely with the local county government officials by providing assistance in valuation questions and property specific information.

X. ADMINISTRATIVE RULES RELATED TO REAPPRAISAL

The department's 2017-2018 Montana Reappraisal Plan, Appraisal Guide and 2017-2018 Montana Agricultural Land Classification Manual have been adopted in the following Administrative Rules of Montana (ARM) and are available at revenue.mt.gov.

- ARM 42.18.122 2017-2018 Montana Reappraisal Plan, Appraisal Guide, and 2017-2018 Montana Agricultural Land Classification Manual
- ARM 42.18.134 2017-2018 Residential and Commercial Reappraisal
- ARM 42.18.135 2015 Forest Land Reappraisal
- ARM 42.18.136 2017-2018 Industrial Property Reappraisal
- ARM 42.18.137 Agricultural Land Reappraisal

XI. PERFORMANCE ANALYSIS

The department's measure of performance is based upon the International Association of Assessing Officers (IAAO) standards. The IAAO standard requires an acceptable median assessment ratio between 0.90 to 1.10, 1.00 is market value. The department also complies with Standard 6, Mass Appraisal, of the Uniform Standards of Professional Appraisal Practice (USPAP).

XII. INFORMAL CLASSIFICATION AND APPRAISAL REVIEW (FORM AB-26) AND FORMAL APPEAL PROCESS

The informal classification and appraisal review process allows the department to take a closer look at a particular property and determine whether the valuation is accurate based on new or previously unknown information provided by the property owner. Property owners also have the right to file a formal appeal to the County Tax Appeal Board (CTAB) and the Montana Tax Appeal Board (MTAB) neither of which are affiliated with the department.

A. Request for Informal Classification and Appraisal Review (Form AB-26)

The Form AB-26 process allows property owners an opportunity to explain to the department why the value shown on their classification and appraisal notice may be incorrect and gives the department the opportunity to address the taxpayer's concerns. A Form AB-26 must be completed and returned to the department's local revenue office as shown on the classification and appraisal notice within 30 days after the date on the classification and appraisal notice. Form AB-26s are available in the department's local offices or online at <http://revenue.mt.gov/home/property/appeal-process.aspx>.

The department encourages property owners who have questions or concerns about their property values to use the informal review process. A complete list of the addresses and telephone numbers for the department's 56 local offices can be found at revenue.mt.gov/home/property/contact-us.aspx. Any taxpayer who has received a

classification and appraisal notice for class three and class four properties and has questions or does not agree with the department's classification or valuation may file a Form AB-26. The property taxpayer, representative, or power of attorney may complete the Form AB-26.

A property taxpayer owning the following types of property may request an informal classification and appraisal review:

- Class Three properties include agricultural land, one-acre homestead on agricultural land, non-productive patented mining claims and non-qualified agricultural land.
- Class Four properties include residential, commercial and industrial land and improvements, including improvements on agricultural land. Also included are one-acre homesteads on forest and non-qualified agricultural land, mobile homes, manufactured homes and golf courses.

Property owners can only submit a Form AB-26 once per appraisal cycle. A separate Form AB-26 should be filed for each separately assessed parcel.

For residential, commercial, agricultural and industrial property, property owners have only 30 days from the date on the classification and appraisal notice to file a Form AB-26 and be eligible for a reduction in value in both years of the two-year appraisal cycle. If the Form AB-26 is not received within the 30-day time period, any reduction in value resulting from the department's review will be applicable only for the second year of the two-year appraisal cycle.

For any pending Form AB-26 informal reviews or formal appeals, Montana law requires the property owner to pay the disputed taxes under protest to receive any refund and accrued interest. The protest must be filed with the county treasurer in writing, specifying the grounds for protest and the taxes must be paid by the due date. Property taxes are billed and collected by the local county treasurer.

B. County Tax Appeal Board

If a property taxpayer is not satisfied with the results of their informal classification and appraisal review, or if they do not want to use the informal review process, they may appeal their value to the County Tax Appeal Board (CTAB) in the county in which the property taxpayer's is located.

Appeals to a CTAB must to be filed within 30 days from the date on the classification and appraisal notice or, if the property owner requested an informal classification and

appraisal review, within 30 days from the determination date on the Form AB-26 decision. Appeals to CTAB must be filed with the property owner's local county clerk and recorder's office, who forwards their appeal to the CTAB secretary to schedule an appeal hearing. Appeal forms are available in local county Clerk and Recorder's offices and on the Montana Tax Appeal Board's website at <http://mtab.mt.gov/>.

Industrial property owners may appeal the department's determination to the Montana Tax Appeal Board (MTAB) or to the county tax appeal board (CTAB) in the county where the property is located.

C. Montana Tax Appeal Board

The Montana Tax Appeal Board (MTAB) is an administrative board tasked with providing an independent and neutral review of the department's valuation of real property for tax purposes. If a taxpayer is not satisfied with the CTAB's decision, the taxpayer can appeal to MTAB. Appeals to MTAB must be filed within 30 days of receiving the County Tax Appeal Board's decision. MTAB decisions are final, unless appealed to district court.

More information can be found on MTAB's website at <http://mtab.mt.gov/>.

XIII. SOURCES

[Montana Constitution, Art. VIII, Sections 3 and 4](#)

15-1-201, MCA

15-6-133, MCA

15-6-134, MCA

15-6-143, MCA

15-7-102, MCA

15-7-111, MCA

15-7-201, MCA

15-8-111, MCA

ARM 42.18.122

ARM 42.18.133

ARM 42.18.134

ARM 42.18.135

ARM 42.18.136

ARM 42.18.137

ARM 42.22.1301, 1304-1310

Mass Appraisal of Real Property; Robert J. Gloudemans, International Association of Assessing Officers, 1999

Montana Agricultural Land Classification Manual 2017-2018, Property Assessment Division, September 23, 2016

Montana Property Assessment Division Appraisal Guide, September 23, 2016

Property Appraisal and Assessment Administration; Joseph K. Eckert, Robert J. Gloudemans, Richard R. Almy, International Association of Assessing Officers, 1990

Property Assessment Valuation Third Edition; Garth E. Thimgan, International Association of Assessing Officers 2010

Sources continued.

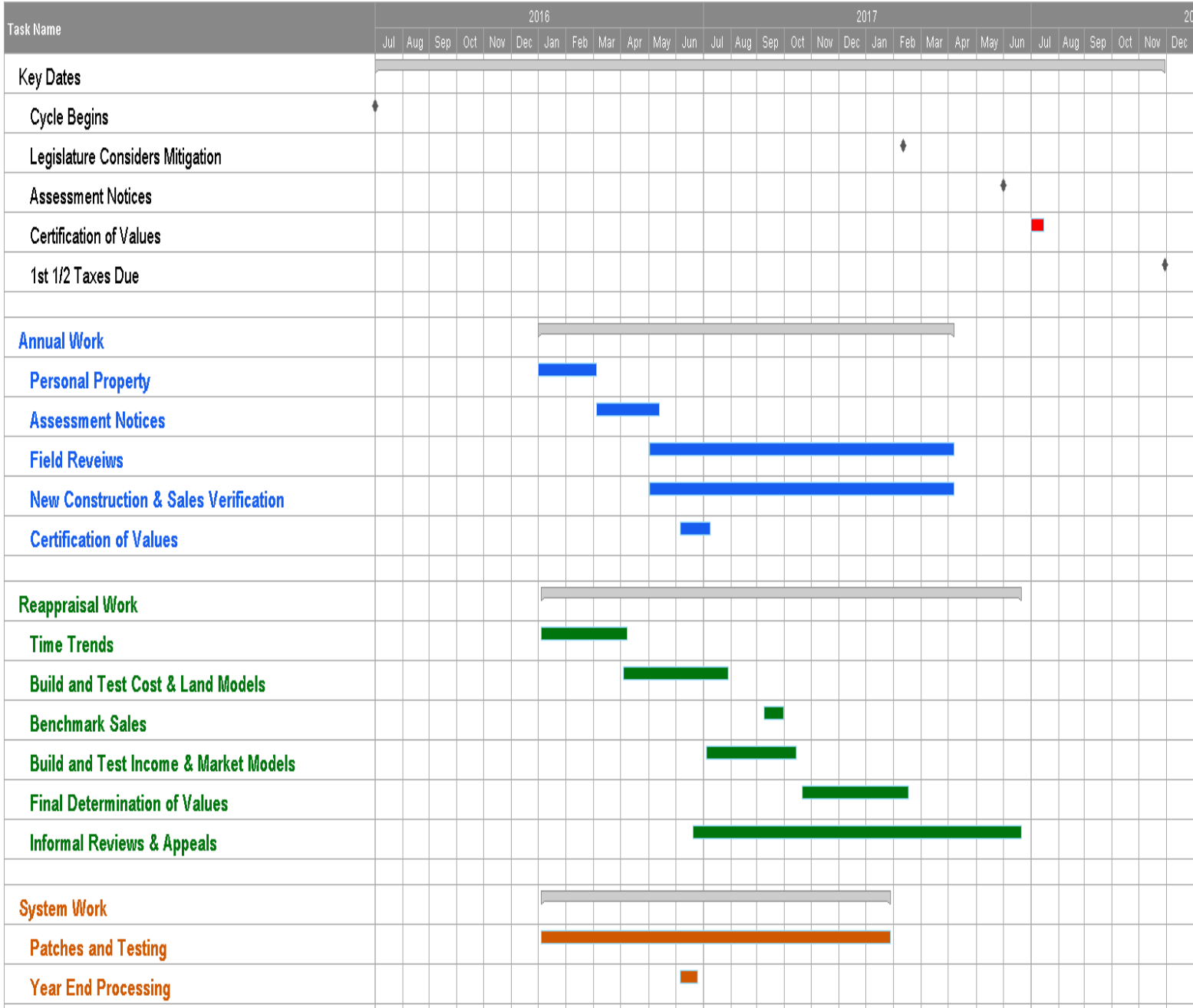
Uniform Standards of Appraisal Practice (USPAP), 2016 – 2017 Edition, Standard 6
Mass Appraisal, Development and Reporting, Appraisal Standards Board

XIV. EXHIBIT A

The following economic areas were identified for the 2017-2018 reappraisal:

- **Flathead, Lake**
- **Cascade**
- **Fergus, Hill**
- **Choteau, Toole, Blaine, Pondera, Teton, Judith Basin, Glacier, Liberty**
- **Missoula, Ravalli**
- **Gallatin, Beaverhead, Madison**
- **Powder, Phillips, Custer, Dawson, Roosevelt, Valley, Big Horn, Richland, Rosebud, Treasure, Sheridan, Daniels, Fallon, McCone, Carter, Prairie, Garfield, Wibaux**
- **Yellowstone, Carbon, Musselshell, Stillwater, Sweet Grass, Wheatland, Meagher**
- **Lewis and Clark, Broadwater, Jefferson**
- **Butte-Silver Bow, Powell, Anaconda – Deer Lodge, Granite**
- **Sanders, Mineral, Lincoln**

XV. EXHIBIT B*



**Subject to change*