

When do I Need a Land Appraisal?

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For the most part, the general public may only encounter the word “appraisal” or an “appraiser” a few instances in their lifetime. This raises the question “when is an appraisal needed?”. To answer this question, it is important to first know exactly what an appraisal is and the process involved.

What is an appraisal?

An appraisal is a report conducted by an appraiser to determine the fair market value of a property as of a specific date. The first step of the process involves a visit to the subject property for a thorough inspection. During the inspection, the appraiser gathers data relevant to the subject and its market area. This information consists of how the land is being used, if there are any buildings on the property, fertility rating, any improvements such as drainage tile or terraces, as well as taking photos of the property.

The next step involves the actual writing of the report. During this step, the appraiser analyzes and describes the subject property, market area, and comparable sales in detail. Detailed income and expense data is collected for the subject and each comparable sale to extract capitalization rates for each sale. A single capitalization rate is then extracted from the group of rates and applied to the net income generated by the subject to derive a value via the Income Capitalization Approach. The Sales Comparison Approach compares each comparable property to the subject with market derived adjustments applied for any differences that are relevant in the market area. The Cost Approach is used mainly if the property is improved with buildings. The cost new of each building is calculated with depreciation subtracted to derive a value for each building. A final reconciliation of all approaches is done to get the final opinion of value for the property.

The following list are the most common reasons for obtaining an appraisal:

1. Financing - Most lenders require an appraisal to be conducted to ensure the property being mortgaged can be sold if the buyer defaults on the loan.
2. Estate Valuation/Tax Planning/Gifting - Many estates are appraised to determine a new tax basis. The date-of-death value is needed for this valuation to calculate capital gains tax at a later date, when beneficiaries sell the property. You also need to know the total value of assets in an estate to determine whether or not the estate will be subject to federal or state tax. Some estates call for heirs to split assets evenly. An appraisal is usually needed to determine the total value and a fair split for each beneficiary. A certified appraisal is also needed for tax planning and gifting purposes. Typically, shares or minority interests in real property are gifted, which transfers wealth to the next generation and ultimately reduces the taxable estate of the donor. A gift made to the next generation may also incur fewer taxes due to the specific person being in a lower income tax bracket.
3. Divorce - The division of assets for divorce settlement needs to be based on the current fair market value of the property.
4. Potential Sale - Owners of real property may wish to obtain an appraisal prior to marketing their property for sale. A certified appraisal is not necessarily needed in this instance, but can be a more reliable valuation as the appraiser must have no bias or future interest in any property being appraised. A broker price of opinion (BPO) is often used if an appraisal is not conducted. A BPO is the estimated value of a property as determined by a real estate broker and is not representative of an official appraised value.

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About the author: Tyler Weaver started his appraisal career in 2014 and has been an Appraiser with Peoples Company since 2019, where he performs valuations on agricultural assets across the Midwest. Tyler is a current member of the ASFMRA Iowa Chapter and can be reached at Tyler.Weaver@PeoplesCompany.com or 855-800-LAND.