



## Rural Valuation Topic #RVT 3: Property Rights

Property rights are the legal rights which are the “subject” of the appraisal. Nearly every valuation course and seminar begins with the concepts of market value and property rights ---- yet, the “property rights” portion is either taken for granted, “check-boxed” away as fee simple, mis-reported or not completely understood.

It is the appraiser’s responsibility to identify the legal rights appraised for the valuation assignment. There are three “base definitions” which must be understood by the appraiser:

1. Black’s Law Dictionary defines fee simple as, “a freehold estate of inheritance”, or translated it means an inheritable estate.
2. Fee Simple Estate (Fee Estate) is “absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the governmental powers of taxation, eminent domain, police power, and escheat”<sup>1</sup>.
3. Encumbrance is “any claim or liability that affects or limits the title to property. An encumbrance can affect the title such as a mortgage or other lien, or it can affect the physical condition of the property such as an easement. An encumbrance cannot prevent the transfer of possession, but it does remain after the transfer”<sup>2</sup>. If the property is leased, the lease represents an encumbrance.

ISSUE: For most properties in rural markets, fee simple seldom occurs. Appraisers are frequently asked to value the “fee simple” estate, but in reality, encumbrances for rights-of-way (roads, powerlines, pipelines, etc.), conservation easements, appurtenant easements, utility pads (wind, solar, power substations, etc.) may exist. If there is/are any reservation(s) after the four limitations originally held by the government after the patent was issued, the property *is encumbered*.

### ASFMRA Recommended Rural Application

**Assignment Condition:** If a client requires the “fee simple” estate to be valued, the appraiser is required to research to see whether that condition exists. If not, there are several options:

- decline the assignment
- notify the client “fee simple” does not exist
- suggest to the client that the legal rights should be identified as the “encumbered fee” and list the encumbrances
  - once the encumbrances are identified, the appraiser should make an affirmative statement as to whether or not the reservations have an impact on value and to what degree
- after thorough sale verification and analysis, the appraiser may

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<sup>1</sup> Appraisal Institute, *The Dictionary of Real Estate Appraisal*, 6<sup>th</sup> Ed., (Chicago: AI 2015, p.90)

<sup>2</sup> Ibid, p. 76

- express their opinion that the “property” has “effective fee” and explain Sales A, B, F, G, H, L, M, and N have similar encumbrances with no evidence they impacted prices, or
- there may be encumbrances that do impact prices to differing degrees --- or from minor to extensive. The appraiser should also identify the sales information that supports that opinion
- there may be both present within the same property, some impacting and some not.

**Stating Appraiser Assignment Definition as “Effective Fee”** (*not a legal term, but an opinion reflecting market impact of encumbrances*): After thorough examination of the market, encumbrances for Sales U, V, W, X, Y, and Z are commonplace. Buyer verifications were undertaken in a consistent manner allowing the buyer to identify which sale elements were positive, neutral, or negative. If all reservations are typical and have a neutral impact, the “remainder rights” can be opined as “effective fee”. The practitioner is presenting an opinion pertinent to the value opinion, i.e., one is contingent on the other. If the encumbrances have a positive or negative impact, those should also be market supported and referenced by sales with the same degree of influence.

#### **Clearly State the Property Rights Appraised**

USPAP Standard Rule 1-2 (e) (ii) states the appraiser must identify the real property interest to be valued. It is imperative the appraiser correctly identify the property rights to be appraised and correctly analyze these rights in relationship to the market data.