

# How Tax Assessors Use the Cost Approach to Value Property

A Fair Assessments, LLC Guide



[www.fair-assessments.com](http://www.fair-assessments.com)



## About the Author

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Daniel Thomas Jones is a property tax consultant at Fair Assessments, LLC which focuses on helping real estate owners minimize their property tax burden.

Before Fair Assessments, he worked for two other property tax management firms. Prior to his work as a property tax consultant, Daniel worked as a mass appraisal specialist at two county tax assessment departments including Fulton County, GA. He is also a licensed real estate appraiser, and has appraised thousands of properties

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## About Fair Assessments

Fair Assessments is a full service property tax reduction firm. When you engage us we will file the appeal on your behalf, do all of the research necessary to build a case for a lower value, and represent you in negotiations with the tax assessment staff and at formal hearings.

Fair Assessments has been in valuation services for 28 years. This has included licensed fee appraisal work, mass appraisal work with two counties, and property tax consulting work for the past 15 years. We have a high value reduction success rate and always get the appeals resolved such that your taxable value is capped for three years.

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# 1

## Market Value

All states base their assessed value on fair market value (also referred to as “market value”), or a defined percentage of fair market value (here in GA we are assessed at 40% of the fair market value estimate).

Market value can be defined as: The most probable price that a property would sell for on a specific date, in terms of cash, and provided that the property is exposed to the open market, and the buyer and seller are both acting in their own best interests and are not under any undue pressure. Every state can have their own market value definition, but they all have all or most of the elements of the definition above.



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## 2

# The Cost Approach

The cost approach is one of three recognized approaches to value.

The cost approach is based on the principle of substitution – that you wouldn't pay more for a property than the cost to acquire a similar site and construct a building of equivalent utility within a reasonable time-frame.

The cost approach estimates the cost to construct the building of equivalent utility, deducts an amount for depreciation on the subject property being valued, and adds land value.





replacement cost services base their data on real construction project data

The cost approach is used by most taxing jurisdictions for residential and commercial properties because it is relatively easy to automate. The cost approach estimates the replacement cost new of the property, or the cost to build a structure of equivalent utility (functionality) using today's construction standards.

Reproduction cost new estimates the cost to build an exact replica, and is rarely used. From replacement cost new an estimate of total accrued depreciation (physical, functional, external) is deducted from the cost estimate to get a depreciated replacement cost new. To that an estimate of the site (land) value is added to get an estimate of the fair market value of the property.

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# 3

## Cost Components

The Tax Assessor's mass appraisal software uses cost data from a national cost data supplier/source. The replacement cost new that they typically use is a basic cost per square foot of floor area. This basic cost per foot is then adjusted by subjective quality of construction and condition ratings.

There are separate cost tables within the mass appraisal database for items such as basement, garages, pools, sheds, etc. that are not included in the base cost per foot.



a quantity survey compiles the cost of every single component down to the nails



physical deterioration is something  
we are all familiar with

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## 4

# Depreciation

Depreciation is another component of the cost approach. First you estimate what it would cost to replace the structure to be appraised, then you depreciate that cost new to get an indication of the current contributory value of the improvements to the total property value.

Physical deterioration is the form of depreciation that most people are familiar with. This results from age, neglect, and lack of maintenance or renovation.

Functional obsolescence is another form of depreciation and can be caused by a deficiency or super adequacy in design. External obsolescence comes from outside of the property, such as noise from a busy road or airport.

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# 5

## Land Value

Land is valued as if vacant and available to be put to its highest and best use. This is often constrained by zoning laws, so that in a residential subdivision all that is legally permissible is single family housing.

Land is often valued via sale comparison, or comparing the subject parcel to parcels that have sold and are similar in size, shape, topography, and zoning.

In the absence of sufficient sales data the tax assessors will often use allocation. If it can be shown over time, that on average, land values represent approximately 30% of total value in residential developments, then that will be a benchmark that they use to value land.

An aerial photograph of a suburban residential neighborhood. The houses are mostly two-story, with grey roofs and light-colored siding. There are green lawns, trees, and paved streets. A semi-transparent red rectangular box is overlaid on the center of the image, containing white text.

when land sales are rare,  
assessors use allocation

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## 6

# The Total Value Estimate

The cost approach value estimate is completed when you deduct an estimate of the total accrued depreciation of the subject property from the replacement cost new estimate and then add your land value estimate. The resulting value is the total value estimate.

The tax assessors will always check their cost approach values on those properties that have sold recently. If the properties that have sold in a particular market area, on average, are assessed at 80% of their sale prices, then the assessors will assume that all tax assessments in that market area are too low.



high land values make  
building up cost effective

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# 7

## An Important Point

***“The quality and condition ratings in the cost approach are subjective.”***

Most properties are assigned to a quality or construction class which tells the computer assisted mass appraisal system (CAMA) what level of replacement costs to use. When neighborhoods are new, typically the properties in them are put in the system with the same quality codes.

Over time however, due to appeals or description updates, these quality ratings begin to change per property. Thus, you may find that your neighbor, who appealed his value last year has a quality code of “B” and your house, built by the same builder in the same year, has a quality code of “A”.