



MONTANA DEPARTMENT OF REVENUE

Industrial Properties Valuation and Timeline

Revenue and Transportation Interim Committee
Senate Joint Resolution 23

September 14, 2017

Industrial Property Appraisal and Timeline

- Generally discuss the appraisal process and timeline:
 - Industrial property description
 - Industrial property classification and market values
 - The appraisal process and timeline
 - Industrial property appraisal/assessment example
- Specifically discuss the appeal process
 - Current Industrial Appeals

What is Industrial Property?

- Industrial property is:

Property used in:

- the extraction of and/or changing the form of raw materials
- production, distribution or assembling components and parts including the packing, warehousing and shipping of the finished products

A property is evaluated on the use, process, complexity and capital investment by the department to determine if it is classified as industrial or commercial property.

Includes all land, improvements to land, buildings, machinery and equipment

- Examples of Industrial Property:

Oil refineries, sawmills, light manufacturing, grain handling facilities, flour mills, coal and metal mines, pharmaceutical manufacturing, high-tech manufacturing, energy production

Industrial Property Classification and Values

	Property Class (Tax Rate)	2017 No. of Properties	2017 Market Value
<u>Industrial Property:</u>			
Real Property	4 (1.89%)	-	\$1,848,263,531
Pollution Control Property	5 (3%)	-	101,995,565
Personal Property	8 (3%)	-	4,117,612,237
Electric Generation Property	13 (6%), 14 (3%)	-	257,174,541
Carbon Sequestration Property	15 (3%)	-	<u>180,420,868</u>
Total Industrial Property		8,839	\$6,505,466,742
<i>Total Statewide Market Value of all Property</i>			\$150,348,839,225
<i>Percent of Total Statewide Market Value</i>			4.33%

** The tax rates are to be used as a general indicator and are not taking into consideration specific exemptions, incentives and abatements that taxpayers qualify for.*

The Appraisal Process and Timeline for Industrial Property

- All property is appraised as of January 1 (lien date)
- All property is appraised using the cost, income and market approaches when appropriate information is available
- **Industrial Property Timeline:**
 - Real property (improvements and land) is appraised cyclically (same cycle as all class 4 property)
 - Established by the Legislature
 - Currently every 2 years
 - Personal property (machinery and equipment) is valued annually
 - Personal property reports are available *January 1* and due *March 1*
 - Appraisals and informal reviews are conducted from *April* through *August* of each year
 - Values are certified with all other property; first Monday in *August*

Three Approaches to Value Industrial Property

Three Approaches to Determine Market Value:

Cost Approach:

- Real Property – Appraisal Cost Tables
- Personal Property – Trending and Depreciation Tables
- Source of Information: Property owner's balance sheet, other audited records, fixed asset lists, site maps, engineering records
- This approach is used in the majority of appraisals due to the lack of information provided to complete an income approach

Income Approach:

- The income approach is considered the best approach for income producing properties
- Discounting an income stream
- Source of Information: Property owner's income statement and financial markets

Market Approach:

- Comparable sales of like property
- Source of Information: Comparable property sales price and data

Industrial Property Appraisal Example

Western Manufacturing Company

- The following slides provide a simple example of the appraisal and assessment process for a hypothetical manufacturing company.
- The example is of a fictitious company and situation.
- The example is meant to illustrate how the appraisal and assessment process works for industrial property facilities.
- It is in no way meant to determine the true result of an appraisal for any actual company or any actual situations.

Western Manufacturing Company

Company Facts:

- Owns a manufacturing facility in Yellowstone County
- Files with the Department:
 - Annual Report – includes updates from prior year’s report
 - Copy of fixed asset list for all personal property and materials and supplies on its balance sheet
 - Other audited financial information as needed: SEC 10-K, regulatory filings, maps, blue prints, etc
- Appraisal is for tax year 2017 (lien date January 1, 2017)

Western Manufacturing Company

Cost Approach

Personal Property - Installed Cost and Installation Date:

Manufacturing Equipment	
20 year life, trended to the current dollar	\$ 17,550,000
Materials and supplies	\$ 80,000
Construction work in progress	\$ 5,000,000
Less depreciation (Physical, Functional and Economic Obsolescence)	<u>\$ (2,750,000)</u>
Cost value of <i>personal</i> property less depreciation	\$ 19,880,000

Western Manufacturing Company

Cost Approach Continued

Real Property Improvements and **Land** - Replacement New:

Warehouse Building: 30,000 sf engineered steel	\$ 5,000,000
Manufacturing Building: 45,000 sf engineered steel	\$ 7,500,000
Land	\$ 2,000,000
Site Preparation	\$ 1,000,000
Other (architecture, legal, permitting, etc.)	\$ 500,000
Less depreciation (Physical, Functional and Economic Obsolescence)	<u>\$ (6,000,000)</u>
Cost value of real property and land less depreciation	\$ 10,000,000

Western Manufacturing Company

Cost Approach Continued

Summary of Cost Approach:

Personal Property	\$ 19,880,000
Real Property Improvements and Land	<u>\$ 10,000,000</u>
Total 2017 Cost Approach to Value	\$ 29,880,000

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Income Approach

Capitalization of Income:

Net operating income:

Year-end 2016	\$ 3,900,000	
Year-end 2015	<u>\$ 3,600,000</u>	
– Average net operating income		\$ 3,750,000

Capitalization rate ÷ 10%

Income value before intangible personal property \$37,500,000

Western Manufacturing Company

Comparable Sales Market Approach

- Sales must be verified as valid - meaning there must be an arms-length transaction
- Information required to verify sales:
 - Marketing period, between related parties, continue to be used at highest and best use, not under duress, etc.
 - Sufficient comparable sales to arrive at logical and accurate adjustments to the comparables e.g. size, location, sales date, etc.
 - Generally, industrial facilities are special purposes properties and finding and accurately adjusting comparables can be very difficult.

Reconciliation

- To arrive at a final value estimate, the appraiser must analyze the results of the various approaches to value and consider the strengths and weaknesses of each approach. This process of examining and resolving the differences among the various value indicators is called reconciliation or can also be referred to as correlation.
- There are many considerations that must be made when reconciling the indicators of value. Two of the most common considerations are:
 - Availability of data to complete each indicator
 - Quantity and quality of the components that went into each indicator
- Lack of reliability and the degree of applicability of each approach to the type of property being valued will cause differences in value indicators that must be reconciled.
 - Simply averaging value indicators is not a proper method since it would imply that all value indicators are equally valid, and this is rarely true.
 - For example, if a property is income producing, an income approach is often given significant weight. Yet, if a property is newly constructed a cost approach may be more meaningful as there is no historical income stream to consider.

Western Manufacturing Company

Reconciliation of the Indicators

Approach	Source	Value	Weight
Cost Approach	Page 11	\$29,880,000	30%
Income Approach	Page 12	\$37,500,000	70%
Market Approach	Page 13	N/A	0%

Reconciled Market Value \$ 35,214,000

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Tax Calculation

Assessed Market Value for Facility <i>page 15</i>	\$35,214,000
Taxable Value Rate <i>(class 4 and class 8 blended tax rate)</i>	<u>2.32%</u>
Taxable Value	\$816,964
Mill Levy	<u>.600</u>
Estimated taxes <i>(mill based taxes only)</i>	<u>\$490,179</u>

The Appeal Process for Commercial and Industrial Property

Standard Valuation Appeal Process:

- Business and Income Taxes Division (DOR) – Informal (aka AB-26)
- County Tax Appeal Board (CTAB) – Formal – Companies can opt to bypass CTAB and proceed directly to Montana Tax Appeal Board (MTAB)
- Montana Tax Appeal Board (MTAB) – Formal
- District Court – Formal
- Montana Supreme Court – Formal

Current Industrial Appeals

Company	Location	Tax Year	Appeal Status	DOR Market Value	Requested Market Value	Protested Taxes
CHS Refinery	Laurel	2014	MTAB	\$848.6 M	\$100.0 M	\$8,099,942
CHS Refinery	Laurel	2015	MTAB	\$820.9 M	\$347.0 M	\$6,124,270
CHS Refinery	Laurel	2016	MTAB	\$936.6 M	\$349.0 M	\$6,712,592
CHS Refinery	Laurel	2017	AB-26	\$967.7 M	\$361.8 M	-
Phillips 66 Refinery	Billings	2016	MTAB	\$614.7 M	\$423.0 M	\$2,993,280
Phillips 66 Refinery	Billings	2017	AB-26	\$685.2 M	\$368.0	-
Calumet Montana Refining LLC	Great Falls	2017	AB-26	\$424.1 M	\$230.0 M - \$250.0 M	-

*Tax bills have not been generated for 2017, yet the anticipation is there will be additional protested taxes in November

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