

Buildings on Land - Do They Contribute Value?

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Buildings, sometimes referred to as ‘improvements’ in an appraisal, provide shelter and storage for equipment, livestock and products on a farm. In the modern day of American agriculture, it’s nostalgic to view old photos of farms and understand how these buildings were used years before. As time progresses and technology changes, so does the utility of the buildings and equipment. What was once a large barn or shed in 1971, may not be large enough in 2021 due to the larger standardization of equipment used on farms today.

A typical agricultural appraisal problem to solve on farms is figuring out if these buildings contribute to the real estate’s overall value. “Land is immobile, and each parcel is unique in its location and composition. Land is durable as a long-term asset, but the supply of land is finite. Land is not only an economic concept, but also a valued commodity to people.” as defined by: *Basic Appraisal Principles*, 2009. Depending on where the land is located can determine how it is used. Climate, topography, and other raw components of land determine if there is viable use beyond vacant land.

Land is an appreciating asset, whereas buildings are a depreciating asset that may or may not contribute value to the real estate property. “Buildings are appurtenant to land. Appurtenance: When improvements or buildings are added to a property and has since become an inherent part of the property; usually passes with the property when title is transferred.” (*Basic Appraisal Principles*, 2009).

Buildings are affected by the three forms of depreciation:

1. Physical deterioration
2. Functional obsolescence
3. Economic obsolescence

Physical depreciation is related to the age and condition of a building and how well maintained the structure is. Typical agricultural use buildings have a physical life of 25-40+ years.

Functional obsolescence is related to the utility of the building in the current or proposed use.

Economic obsolescence is related to the microeconomic and macroeconomic influences that support the enterprise on the farm (e.g. dairy, swine, grain production).

Physical depreciation is deducted by using the straight-line method based on the useful and total economic life of the improvements. Comparable property sales in the market with similar structures are used to extract functional and external obsolescence from the market and apply them to the improvements on the subject property. Functional and external obsolescence are combined many times since the market struggles to differentiate between the two forms of obsolescence.

In a typical appraisal report, the physical, functional, and economic attributes of a building(s) are analyzed. The current intrinsic value of the building(s) to the property owner are noted, but they may not always have the same value to a different property owner. A common phrase in an appraisal report is: "These buildings may have value in use, but do not have value in exchange." This is further analyzed and defined in the appraisal of the property. The analysis of comparable sales data of similar properties with similar structures help define the market value and apply less subjective value.

Take for example: An upright silo on a dairy farm. These structures were common across the Midwest for feed storage, especially in the 1970's and 1980's for smaller dairy farms. Many times, multiple silos were built for additional silage and feed storage as the dairy grew. Their physical use, if they were maintained, could age the structure to succeed 30+ years. As technology on farms have progressed and dairy farm buildings have changed over the years, the function and economic viability of an upright silo have significantly declined. What once was an icon for many dairy farms in yester-year, are now rarely used due to the more modern and typical feed storage use of 'bunker silos'.

The intrinsic value of buildings to a property owner can be interpreted differently depending on the market of where the property is located, how old the buildings are, and the goals the property owner has for the property's future use. An appraisal of the market value of real estate shows the data derived from depreciation of these building(s) and how much market value they contribute to the property.

Peoples Company's appraisal division specializes in agricultural valuations including cropland, recreational and agribusiness properties. For more information about how buildings may impact the value of a particular property, contact a Peoples Company Appraiser at Appraisal@PeoplesCompany.com or call 855.800.5263.