Golf Course Valuation – The Income Approach
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Today We Will Cover

- Basic Definitions and Information
- Other Valuation Methods
- Appeal Process
- Annual Adjustment
- Circuit Breaker
Golf Course Valuation – The Income Approach

The Income Capitalization approach is one of three approaches to the valuation of real property. The appraiser derives a value indication for income-producing property by converting the anticipated benefits through ownership of property. (Source: International Association of Assessing Officers – Course #102 “Income Approach to Valuation”).

It is based on the economic principles of:
- Anticipation
- Change
- Supply and demand and competition
- Substitution
- Balance and contribution

Real estate competes with other investments for the investor’s dollars. All investors want a return on their investment. All investors want a return of their investment.
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- **“IRV”** – A Generic Capitalization Formula
  - I (income) = Rate x Value
  - R (rate) = Income/Value
  - V (value) = Income/Rate

- For example, a corner lot in a business district is used as a parking lot. The monthly income earned is $1,250. The owner’s required rate of return for this type of property is 7.5% per year. What is the value of this property?

  Monthly Income $1,250
  \[ \times 12 \]
  Annual Income $15,000

  IRV Formula: \( V = \frac{I}{R} \)
  \[ \frac{15,000}{.075} = 200,000 \]

  Capitalization can be defined as the process to convert income into an estimate of value.
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- **Basis of Income:**
  For a golf course, there may be several different sources of income, including green fees, membership dues, pro shop, concessions, and other miscellaneous sources.

- **Income and Expense Statement:**
  Reconstructed from the owner’s statement. Format:
  - Gross Income Estimate (potential gross income)
  - Vacancy and collection loss (derived from market)
  - Miscellaneous Income
  - Effective Gross Income
  - Allowable Expenses
    - Operating
    - Replacement Reserves
    - Real Estate taxes (deducted under certain conditions)
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- **Allowable Expenses:**
  - Management fees/expense
  - Insurance
  - Salaries
  - Benefits
  - Utilities
  - Advertising
  - Repairs
  - Supplies
  - Legal and Accounting Fees
  - Miscellaneous Expenses
  - Replacement Reserves
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- Non-allowable expenses:
  - Depreciation (reflected in the recapture rate)
  - Capital improvements
  - Franchise fees and special corporation costs
  - Owner’s personal expenses (income taxes, etc.)
  - Debt service (principal and interest on mortgage)
  - Payments on loans for capital improvements
  - Real Estate taxes (not deducted as an expense under certain conditions – reflected in the effective tax rate).

- Total Operating Expenses
- Replacement Reserves
- Total Expenses

- Net Operating Income
## Golf Course Valuation – The Income Approach

### Income and Expense Statement for the Duffer’s Paradise Golf Course:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Income</td>
<td>$500,000</td>
</tr>
<tr>
<td>Collection Loss (estimate 2%)</td>
<td>&lt;$10,000&gt;</td>
</tr>
<tr>
<td>Effective Gross Income (EGI)</td>
<td>$490,000</td>
</tr>
<tr>
<td><strong>Expenses:</strong></td>
<td></td>
</tr>
<tr>
<td>Management (5% of EGI)</td>
<td>$24,500</td>
</tr>
<tr>
<td>Employees’ salaries</td>
<td>$80,000</td>
</tr>
<tr>
<td>Employees’ benefits</td>
<td>$2,500</td>
</tr>
<tr>
<td>Insurance</td>
<td>$10,000</td>
</tr>
<tr>
<td>Utilities</td>
<td>$4,000</td>
</tr>
<tr>
<td>Water</td>
<td>$10,000</td>
</tr>
<tr>
<td>Repairs</td>
<td>$12,000</td>
</tr>
<tr>
<td>Supplies (e.g. seed, fertilizer)</td>
<td>$300,000</td>
</tr>
<tr>
<td>Legal &amp; Accounting Fees</td>
<td>$4,000</td>
</tr>
<tr>
<td>Miscellaneous Expense</td>
<td>$3,000</td>
</tr>
<tr>
<td><strong>Total Expenses</strong></td>
<td>$450,000</td>
</tr>
<tr>
<td><strong>Net Operating Income (NOI)</strong></td>
<td><strong>$50,000</strong></td>
</tr>
</tbody>
</table>
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**Capitalization Rate:**

Determining the Net Operating Income is a key determinant in establishing the value of a property in the income approach. The other key component that can have a significant effect on the total value of the property is the capitalization rate.

We will focus on the “Overall Capitalization Rate” (OAR) which expresses the relationship between net operating income and the market value of the property.

It can be developed using the following:
- Market Extraction
- Effective Tax Rate
- Mortgage & Equity
- Discounted Cash Flow
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Capitalization Rate continued:

- Contrary to popular belief, the OAR is not always “10”!
- The OAR reflects risk, liquidity (or lack thereof), potential for growth in net income, and general requirements of the investor.
- To determine the value of the property (simplistically), divide the Net Operating Income by the Overall Rate.
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- **Duffer’s Paradise Golf Course:**
  For example (using our previous NOI):
  - $50,000 divided by a 7% OAR = $714,286
  - $50,000 divided by a 10% OAR = $500,000
  - $50,000 divided by a 12% OAR = $416,667

So now that we know the capitalization rate can have a significant impact on the value of the property, what other things can make a difference?

- Replacement Reserves: This allows a fund to be collected to replace items that will wear out. For example, an apartment complex may establish a replacement reserve for the roof, furnace, water heater, carpet, etc. These items are deducted after the operating expenses (included in the total expenses).
- For a golf course, these items could possibly include a roof for the clubhouse, a water heater, furnace, etc.
- The amount of income and expenses are the other things that will obviously have an impact on the bottom-line.
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- **Steps to Determine Value:**
  - Determine Potential Gross Income
  - Calculate Vacancy & Collection Loss, plus miscellaneous income
  - Effective Gross Income
  - Deduct Expenses and Replacement Reserve
  - Net Operating Income
  - Capitalize
  - Does one size fit all – not necessarily!
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- Other Valuation Approaches: Cost Approach

2002 Reassessment Guidelines (see attachment – developed from Marshall & Swift)

- Data Collection of Courses:
  - Clubhouse
  - Facilities/Pool/Tennis
  - Parking
  - Maintenance/Support Buildings
  - Tees – Size/Difficulty/Stations per hole
  - Fairways – Width/Irrigation Type/Grass Type/Condition
  - Bunkers – Size/Number/Difficulty
  - Greens – Size/Number/Condition
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- Data Collection of Courses continued:
  - Rough – Irrigation Type/Area
  - Practice Facilities – Size/Maintenance
  - Number of Rounds played for last three years
  - Fee Schedule
  - Public vs. Private?
  - Who was the architect?
  - Last major renovation?
  - Initiation fees/dues (Social only)?
  - Obtain Scorecard (Should have par & slope)
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- **Guidelines Pricing Sheet:**
  - Price by grade per hole
  - Delete land under course value @$1,050 per acre
  - Apply the appropriate physical and/or external depreciation
  - Add value of other improvements
  - Add land value
  - Adjust to Market Value-in-Use

Grade AA (Base Cost - $163,000 per hole)
- Superior Quality, Professional Championship Design
- 18 holes on 180 acres
- Rolling and/or lake terrain
- 7,200 yards long
- Rated par of 72
- Automated sprinklers, 10,000 sq. ft. tiled greens, 3 tees per hole
- Average 3 bunkers per hole
- Good quality paved roadways
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Grade A (Base Cost - $118,000 per hole)
- Excellent quality, designed for championship play
- 18 holes on 160 acres
- Rolling and/or lake terrain
- 7,200 yards long
- Rated par of 72
- Automatic sprinklers, 8,000 sq. ft. tiled greens
- 2 or 3 tees per hole, average 3 bunkers per hole
- Good quality paved roadways

Grade B (Base Cost - $73,000 per hole)
- Good quality private club
- 18 holes on 130 acres
- Rolling terrain
- 6,400 yards long
- Rated par of 70
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Grade B continued:
- Automatic sprinkled greens, manual fairway sprinkled
- 5,000 sq. ft. tiled greens, 2 tees per hole
- Average 2 bunkers per hole
- Good quality paved roadways

Grade C (Base Cost - $50,000 per hole)
- Average quality public or municipal type course
- 18 holes on 110 acres
- Primarily flat terrain
- 6,000 yards long
- Rated par of 67 to 70
- Semi-Automatic sprinkler system
- Small tees and greens with few bunkers
- Average quality paved or gravel roadways
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Grade D (Base Cost - $23,000 per hole)
- Fair quality course
- 18 holes on 90 acres
- Flat terrain
- 5,400 yards long
- Rated par of 64 to 67
- Manual sprinkler system
- Small tees and greens with few bunkers
- Gravel roadways

Short Play Courses:
Executive Course (Base Cost - $44,400 per hole)
- 18 holes on 50 to 60 acres
- 4,600 yards long with sprinklers
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Short Play Courses continued:
Par 3 Course (Base Cost - $30,000 per hole)
- 18 holes on 30 to 40 acres
- 2,800 to 3,000 yards long with sprinklers

Pitch and Putt Course (Base Cost - $22,800 per hole)
- 9 holes on 10 to 15 acres
- 1,400 to 1,500 yards long with sprinklers

Golf Course Land Values:
- Determine the number of acres under the holes
- Multiply by $1,050 (or the value prescribed by the DLGF)
- Subtract that amount from Golf Course hole value
- Apply $1,050 per acre to the land value portion of the parcel
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Pricing Example:

“B” Grade, 18 holes, 126 acres, Built in 1980, “Average” Condition

- $73,000 x 18 = $1,314,000
- 126 acres x $1,050 = $132,300
- $1,314,000 - $132,300 = $1,181,700
- 15% Depreciation (From the Guidelines – see http://www.in.gov/dlgf/local/realproperty.html) = $1,004,400
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Sales Comparison Approach:

The third approach or method in determining the value of real property is the sales comparison approach. It estimates the total value of the property directly by comparing it to similar, or comparable, properties that have sold in the market.

All three approaches (Income, Cost, and Sales Comparison), when properly processed, should produce approximately the same estimate of value. Fee appraisers use all three approaches when appraising individual properties. However, assessing officials are faced with the responsibility of valuing all properties within their jurisdictions during a reassessment and often times do not have the data or time to apply all three approaches to each property.

So, what should you do if you believe the assessed value (not the amount of property taxes) is incorrect?
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Appeal Procedures:

Indiana law provides a couple of ways for taxpayers to contest the assessed value of their property. Both begin at the local level and can be appealed to the state only after being reviewed locally.

One way begins with written notification to the township assessing official requesting an informal conference to discuss the assessment. The request should detail the pertinent facts of why the assessed value is being disputed. It should also include the parcel number, property address, property owner name and contact information. A taxpayer may only request a review of the current year’s assessed valuation.

Following the informal conference with the local assessing official, the township assessor will make a recommendation either denying or approving the appeal. If denied, the township will forward the appeal to the county Property Tax Assessment Board of Appeals (PTABOA) for review. If the PTABOA denies the appeal, instructions will be provided on appealing the decision to the Indiana Board of Tax Review.
The other appeal process begins with the submission of a Petition for Correction of Error (Form 133) to the County Auditor. This form may be used to appeal objective issues such as:

- The taxes are illegal as a matter of law.
- There is a math error on the assessment.
- Through error or omission by any state of county officer, the taxpayer was not given credit for an exemption or deduction as permitted by law.

Claims may be made for up to three years of assessments with the submission of the Form 133. However, taxpayers requesting refunds must also file a Claim for Refund form (Form 17T).

In order to appeal a current assessment and have a change in the assessment effective for the most recent assessment date, the taxpayer must request a conference with the local assessing official not later than forty-five days after notice of a change in the assessment is given to the taxpayer or before May 10, whichever is later.
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Appeal Procedures continued:

A Form 133 must have the approval of at least two of the following officials: the county auditor, county assessor or the township assessor. If the petition is denied, the county auditor shall refer the matter to the PTABOA for determination. The PTABOA shall provide a copy of their determination to the petitioner and the auditor.

A petitioner may appeal the PTABOA decision to the Indiana Board of Tax Review. The appeal must be made within thirty days after the mailing date of the PTABOA determination, and is filed with the county auditor.

After being heard by the Board of Tax Review, taxpayers may also seek review by the Indiana Tax Court. Details on how to appeal to the Tax Court following review by the Board can be obtained by contacting the Indiana Board of Tax Review.
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Annual Adjustment:

Overview:
Annually adjusting property values are part of Indiana’s move to a market-based assessment system that began in 2002. Similar market-based assessment systems are currently being used in 48 other states.

The annual adjustments are calculated by comparing the prior year assessment with current sales data from a neighborhood. The difference, positive or negative, will be used to create a factor that assessing officials will apply to the property’s assessed value to bring it to current market value.

Under the old system, real estate was generally only reassessed every 10 years. That left taxpayers with a large change in their assessments every decade. Annual adjustments curb that large lump sum change in assessments by annually adjusting values based on sales.
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Annual Adjustment continued:

Taxpayer Impact:
Hoosier taxpayers could see an increase or a decrease in their tax bills after the annual adjustment of their assessment based on their location and the expenditures by local government. In essence, the assessment represents a property owner’s share of the overall tax burden for a specific area. Because property values rise and fall over time, annual adjustments are necessary to ensure an assessment reflects the current market value of a property. With annually adjusted market-based assessments, the local tax liability in a community will be more uniformly distributed.

Appeal rights don’t change with the implementation of annual adjustments. Taxpayers will still be able to review their assessment and appeal the value of the property to local assessors. It’s important to remember that an increase in the assessment does not necessarily cause an increase in taxes. A person’s tax bill is a direct result of local budgetary needs of their government and schools.
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Annual Adjustment continued:

How It Works:

Property values in Indiana are currently based on assessments made in 2002. Those 2002 assessments were made using a January 1, 1999 value of property. Using annual adjustments, assessors will adjust or “trend” property values every year to reflect market values of property. Officials will use sales data from state-required sales disclosure forms completed during every real estate transaction to calculate how much or how little to adjust the assessed value of a property. The amount of adjustment is determined by how much or how little property increased or decreased in the area. The amount of change is then applied to all assessed values of properties of that type (residential, commercial, etc.) in the area. After applying the annual adjustment factor, the property value is considered adjusted for local market conditions.
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Circuit Breaker:

Overview:
The circuit breaker became law in 2006 with the passage of House Enrolled Act 1001. It is aimed at helping Hoosiers by ensuring they don’t pay more than 2 percent of their property value in taxes. The goal is to provide predictability in tax bills and equity among Hoosier taxpayers.

The Circuit Breaker is slated to become mandatory statewide for residential property in 2007. Homeowners will not see the potential Circuit Breaker impact until their 2008 tax bill. The circuit breaker expands to include all property types in 2009. Taxpayers will not see the impact of the expansion until their 2010 tax bill.
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Circuit Breaker continued:

Taxpayer Impact:
The circuit breaker provides property owners with a credit for any amount of taxes over 2 percent. For example, the maximum amount of property taxes a homeowner would pay on a $100,000 house would be $2,000. In this example, the credit limits the tax liability for the property to the 2 percent cap of $2,000. The impact the Circuit Breaker may have on local governments and taxpayers will not be fully known until the annual adjustments of assessed values are completed later this year. With the new assessed values, counties and the state will be better able to fully calculate the impact of the Circuit Breaker.
Circuit Breaker continued:

**How It Works:**

Once property values are annually adjusted by local assessing officials to reflect current market conditions, counties will establish the 2 percent property tax cap for each property.

For example, the maximum amount of property taxes a homeowner would pay on a $100,000 house would be $2,000, or 2 percent of the property’s assessed value before deductions.

Each unit of government in the county (schools, cities, towns, etc.) then adopts a budget and calculates a tax rate based upon their projected spending. Those tax rates are applied to each property in the county.
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Circuit Breaker continued:

How It Works continued:

If the total tax liability for the property exceeds the 2 percent “circuit breaker,” the county auditor will provide a tax credit for the amount that exceeds the 2 percent. For example, if a property with a gross assessed value of $100,000 has a tax bill of $2,100, the county auditor would give the property owner a $100 credit to reduce the tax bill to $2,000. In this example, the credit reduces the tax liability for the property to the 2 percent cap of $2,000. The credits that the Circuit Breaker provides are aimed at ensuring Hoosier taxpayers don’t pay more than 2 percent of their property’s assessed value in taxes.
Questions

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