



Los Angeles County
Office of the Assessor



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An Overview of the Mills Act Valuation

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Topics this presentation will cover

- Purpose of the Mills Act
- The Assessor's Role
- California Revenue and Taxation Codes
- The required three approaches to valuation of Mills Act properties
- Sample Valuations

Purpose of the Mills Act

- ▶ The Mills Act offers owners of historical buildings the opportunity to realize significant property tax savings in exchange for preserving historical buildings or structures.

Older base years may not benefit from the Mills Act valuation

- The Mills Act program is especially beneficial for recent buyers of historic properties and for current owners of historic buildings who have made major improvements to their properties.

The Assessor's Role

- ▶ The Assessor is required to value a Mills Act contract according to Section 439-439.4 of the Revenue and Taxation Code. The contract becomes effective on the following January 1st (Lien Date) after the contract is signed and recorded.

California Revenue and Taxation Code

Article 1.9. Historical Property--Sections 439-439.4

439.3 (b) The ... Assessor in each year until termination of the period for which the property is enforceably restricted shall do all of the following:

1. Determine the full cash value* of the property pursuant to Section 110.1. (*Current fair market value)
2. Determine the value of the property by the capitalization of income method as provided in Section 439.2.
3. Original Trended Base Value* as defined by R&T Code Section 110.0.
*(Prop 13 value)

Valuation Using the Market Approach

- Determine the value of the qualified historical property on the basis of recently sold, comparable properties as if exposed for sale in the open market (free of contractual restrictions) per R&T code Section 110 (fair market value).
- ▶ For the purpose of this presentation, we estimate the FMV of a 2000sf SFR is \$800,000. The current land value is \$550,000 and current imp value is \$250,000.

Valuation by Income Approach

The valuation is based on the Income Approach. The income approach converts income into value. The annual rental income, vacancy and collections, and expenses of a property are determined using current market information.

Income Approach to Value

- ▶ Scheduled gross annual income (SGAI) is the amount the property could rent for in one year, plus any additional income the property produces
- ▶ Vacancy and collections is the total loss due to vacancies and unpaid rent
- ▶ Effective gross annual income (EGAI) is the (SGAI) less vacancy and collections
- ▶ Expenses allowed are the average annual allocation of money that can be charged against the revenue expected. These are not homeowner's expenses, but a typical landlords expense
- ▶ Net income before taxes & recapture is the effective gross income less expenses
- ▶ Capitalization rate-which consists of the interest component, the property tax component and the amortization component

Derivation of Capitalization Rate

- Capitalization Rate consists of 4 components:
- 1. SBE Interest Component. This component is tied to mortgage interest rates; therefore, can fluctuate annually. Published by the State Board of Equalization.
- 2. SBE risk component for historical property:
 - *4% for owner occupied Single Family Residence.*
 - *2% for all other restricted historical property. This is a fixed component.*

Derivation of Capitalization Rate (Continued)

➤ 3. Property Tax Component

- - *Tax Rate*

➤ 4. Amortization Component

- - *Amortization component is the reciprocal of the estimated remaining economic life (REL) of the improvement multiplied by the ratio of improvement value to land value.*

Example of Deriving Value by the Income Approach

SFR= 2000sf at Market Rent of \$1.80/sf/mo = \$3,600 per month

SGAI = \$3,600 x12 = \$43,200

Less V&C at 3% =(\$1,300)

EGAI = \$41,900

Less exp. @ 20% =(\$8,380)

NIBR&T = \$33,520

- SBE Interest Component for 2016: 4.25%
- SBE Risk Component (SFR): 4.00%
- Imp. to Land Val. Ratio X Bldg. Amort.(1/REL) = (.45 x .025): 1.10%
- $(\$250,000)/(\$550,000) \times 1/40$
- Tax Rate: 1.02%
- **Total Capitalization Rate:** 10.37%

Capitalized Value(Mills Act Value): \$33,520 (NIBR&T) = **\$323,240**
 (Income Approach) .1037 (Capitalization Rate)

Base Year Value Trended

- The base value of a property is the Prop 13 value established for the change of ownership (typically the date you purchased the property) and date of new construction (if applicable) trended up no more than 2% annually.

Valuation of Historical Property (R&T Code Section 439.2)

- When valuing an enforceable restricted historical property, R&T Code Section 439.2 mandates the final valuation be the lesser of the following:
 - 1. Valuation by the Income Approach as defined by R&T Code Section 439.2.
 - 2. Market Approach as defined by the R&T Code Section 110.1414
 - 3. Original Trended Base Value as defined by R&T Code Section 110.0

Reconciling the 3 Approaches to Value

Annual Review as of January 1, 2015

A	Proposition 13 Base Year Value (Trended)	B	Estimated Current Fair Market Value	C	Mills Act Appraised Value	Enrolled Value (Per Mills Act)
Total	\$500,000	Total	\$800,000	Total	\$323,240	Total \$323,240

Determining Final Mills Act Value

- Once all three values are determined, the Assessor enrolls the lowest of the three values and a Mills Act Notice of Assessed Value Change is mailed to the taxpayer and the city.

Mills Act Contract under Non Renewal

- ▶ A contract under Non Renewal is valued annually until the end of the 10 year contract, at which time the trended base value is enrolled.

- ▶ For example: Year 1 of Non Renewal

▶ 2016 Trended Base Value	\$500,000
▶ Capitalized Value	<u>- \$323,240</u>
▶ Remainder	\$176,760
▶ PW1 @ 10 years @ 4.25%	<u>x 0.66</u>
▶ Present worth of the remainder	\$116,616
▶ Capitalized value	+ \$323,240
▶ Assessed Value for 2016	\$439,856

Resources pertaining to Mills Act properties

- For further information regarding the Mills Act valuation and the current historical property interest component, contact the State Board of Equalization—they publish the “Guidelines for the Assessment of Enforceably Restricted Historical properties”.
- Their website is: www.boe.ca.gov.