

Cost Approach Analysis

The Cost Approach Analysis is defined as a "method in which the value of a property is derived by estimating the replacement cost of the improvements and deducting therefrom the estimated depreciation." There are three primary forms of depreciation: physical, functional and economic. Physical depreciation is often curable and may involve cosmetic appearance (but, in fact, could go deeper). Functional depreciation means that the machinery has had a loss in productivity due to wear and tear. Economic depreciation (sometimes referred to as External Depreciation) occurs outside of the subject property which results in a loss of value. In determining depreciation, the appraiser has used her judgment and prudence in determining the depreciation factor which could be a combination of all three forms described in total. Experience with this type of equipment has proven the use of a formula, which is as follows:

$$\text{Fair Market Value} = \frac{\text{Remaining Life}}{\text{Normal Life}} \times \text{Cost New}$$

This formula again has proven to be effective on numerous occasions.

