

Lessons From Louisiana –Appraisers Perspective

Hurricane Katrina hit August 29, 2005 so the people of Louisiana have had nearly three years to see its impact. Shortly after the flood crested and the sandbagging stopped here in the Corridor I looked to Louisiana and their appraisers to better understand our future.

Who gets bought out and how much is paid?

Put simply, the more FEMA has to pay in flood insurance proceeds the higher the likelihood that they will buy out. I counted 123 homes in the Parkview neighborhood. Of this approximately 32 are within the 100 year flood plain and approximately 7 properties were not immediately impacted. The remaining 84 properties are in the 500 year flood plain. The concerns of a homeowner in the 500 year flood plane will diverge from the 100 year owners for the simple reason that very few 500 year owners have flood insurance and most 100 year owners do have it.

FEMA is looking for the most efficient use of the money or the best return. FEMA pays based on the history of prior flooding and likelihood of future flooding. For example, one home in E Baton Rouge appraised at \$121,080 had \$154,644 in previous flood damage from five prior floods. It qualified as one of the top 30 houses for a buy out in that area. FEMA paid 75% of that cost.

<http://www.fema.gov/library/viewRecord.do?id=1792>

According to Mr. Dunbar Argote, MAI, the maximum buy out paid by FEMA in the wake of Hurricane Katrina was \$150,000. To put this into local perspective, the average home sold in Idyllwild since 2003 is about \$227,000. The sales ranged from \$180,000 to \$310,000. One thing we can count on- there will not be enough funds to cover everybody.

A second FEMA program will pay part of the cost to elevate homes out of the Base Flood Elevation. I understand there is an additional \$30,000 which can be used to elevate a home in Johnson County that is paid by flood insurance. The table below summarizes the funds paid a few years back to elevate homes in the DuMonde Subdivision of Jefferson parish. As with buyouts, FEMA provides up to 75% of the cost to elevate but I believe it only applies to those homes that have flood insurance.

| Appraised Value | Prior Damages | Floods | Cost to Elevate | Height Increase In Feet |
|-----------------|---------------|--------|-----------------|-------------------------|
| \$300,000 | \$75,000 | 2 | \$112,300 | 16 |
| \$300,000 | \$510,000 | 3 | \$95,000 | 13 |
| \$375,000 | \$370,000 | 3 | \$145,000 | 18 |
| \$125,000 | \$68,000 | 2 | \$65,000 | 13 |
| \$200,000 | \$94,000 | 7 | \$60,000 | 13 |
| \$75,000 | \$65,000 | 3 | \$60,000 | 18 |

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Performance Analysis, March 5, 2002

What are some other options?

For homeowners or commercial properties without flood insurance, deduction of casualty losses may provide the fastest path to some needed funds. These losses are measured by the difference between the value before the flood and the value after. These losses can be applied to an amended 2007 income tax return and subsequently used to offset income not only from 2007 but if necessary carried forward for the next 20 years. According to Mr. Argote who met with an IRS representative, market wide adjustments to determine home values would not be acceptable. In other words using assessed value plus or minus some factor might not pass muster if you are trying to convince the IRS to approve a Casualty loss. It may work fine if you are establishing a base for the 50% loss rule.

Determining pre flood value is more complex than appraising a typical home that can be inspected and photographed. In order to determine pre flood value, it is necessary to recreate the condition of the home. There is considerable variability in the Parkview neighborhood in this regard. Capital improvements can change the value of a house. While the owner's word is helpful, the cost of a remodeled kitchen must be confirmed either with receipts, building permits or discussions with contractors. The cost of a project seldom translates into full market value and this is something the appraiser needs to consider.

For the value after the flood the situation is considerably more complex. If an after value is required there really is no formula that applies. There are likely to be very few or no comparable sales of flood damaged property. According to Heidi Lee, MAI, comparable sales for the after situation were non-existent shortly after Hurricane Katrina. They used listings, and investors surveys among other methods to help determine after value.

The most reliable method was the cost to cure. The cost to cure involves three stages: 1) **Remediation** – demolition, removal of drywall and damaged furnishings and finish. 2) **Re-creation of the Vanilla Box** - new utilities and ductwork, painted and primed wall board, replaced siding etc. 3) **Cost of final finish** – floor and wall coverings, window treatments, cabinetry etc.

Jean Felts, MAI said, “Be sure to add a storm premium to any construction costs. Our costs were 15 to 25% higher than the Marshall Valuation Manual numbers. Things have moderated a bit but are still above pre-storm \$\$.” Mr. Argote agreed with this assessment and indicated that in the initial phases the cost increases were higher in part because much of the labor force left town.

In estimating the After Value, a key issue is stigma. If a house has been flooded and may flood again, how much of a decrease in value is the market likely to recognize as compared to a house without this problem? Again, this is a subjective judgment but it requires some reasonable documentation in order to pass muster with the IRS.

According to Patricia Williamson, MAI, there may have been a decline in value for repaired homes in moderate and upper income areas but it wasn’t directly attributable to the flooding. I am guessing that the demand for existing homes may have increased because so many were completely destroyed. For the middle and upper income areas, people tended to stay. Demand remained fairly strong and prices after repair remained pretty steady.

In contrast, those in the poor neighborhoods lacked the resources to remain and the demand collapsed, so did the prices. For residential land values, Mr. Argote notes for high income areas... “flooded land values for residential have dropped off 35%. In the poor areas almost no market exists, (for residential land) despite the City’s claim that 50% to 70% of the population has returned.”

Regarding commercial values, Patricia Williams indicated, that while values have gone down as a result of the decline in the tourist business, “I have not seen a huge decrease in property values in the commercial sector otherwise. The loss in inventory kept values from dropping too low.” Mr. Argote notes that the “commercial areas which flooded badly in the poor areas have barely returned, in more prosperous areas, substantial improvement has been made.”

Finally, I sought some guidance to identify bottlenecks in the process. According to Jean Felts, MAI, “I would suggest that you and other appraisers contact clients who may have storm damage and urge timely ordering of appraisals if they will be needed for tax purposes or insurance claims. Perhaps your local media could help on this. ... the clients waited much too long to get on the schedule of the available appraisers.”

The upshot is this. There are big disparities between properties and between homeowners. There is a big difference between commercial properties and residential properties. There is a big difference between poor areas and areas that would not be considered poor. Importantly, there is a big difference between Iowa City and Cedar Rapids and finally there is a significant difference between either City and New Orleans. At the same time, we have a lot in common and there is much to learn from the gathered wisdom of those who experienced a natural cataclysm.

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