nerej CELEBRATING 55 YEARS

MA/RI Chapter of Appraisal Institute’s April message - by Bud Clarke

April 13, 2018 - Appraisal & Consulting

Bud Clarke
Boston Financial
Investment Mgmt.

The month of March recently came in like a lion and out like a lion, not a lamb! New England’s third nor’easter in less than two weeks slammed parts of the region and dropped as much as 2 feet of snow in some places and brought dangerous whiteout conditions on the roads.

Hurricane force wind gusts were severe in places as much of coastal Massachusetts, Rhode Island, Connecticut, New Hampshire and Maine bore the brunt of the storms. Low lying coastal areas experienced significant flooding and damage, while communities all over the region experienced flooding, falling trees, and power outages.

The aftermath of these storms left damaged homes, breached seawalls, and wreckage scattered in the streets, with generator-powered pumps sucking saltwater from flooded basements. Shattered fences and broken trees littered yard after yard.

Disasters tend to occur suddenly, taking the public by surprise, even when the location is known to be prone to such an occurrence. Depending on the nature of the disaster, destruction of property may be widespread and to varying degrees. Initially, the collective reaction to any disaster is shock; however eventually, there is recovery and damaged property needs to be repaired and destroyed property is often replaced.

With these types of storms comes the need for appraisal expertise that can address this damage, dislocation and material changes in real estate market conditions. Demand for appraisal and valuation services will increase, and the assignments likely will be complex and require the services of experienced appraisers. Analyzing data in such markets presents an array of challenges. How can an appraiser develop a credible opinion of market value in the aftermath of a disaster?

AI’s Guide Note 10: Development of an Opinion of Market Value in the Aftermath of a Disaster can help appraisers servicing areas affected by catastrophic events. In recent years, the northeast has experienced several unusually destructive hurricanes, floods, and severe winter storms. During such periods, real property markets in affected areas often exhibit instability, and sometimes chaos. Analyzing market data in such markets can be problematic.

The purpose of Guide Notes to the Appraisal Institute's Standards of Professional Appraisal Practice is to provide guidance as to how the requirements of the Standards may apply in specific situations.

The four key concepts of AI's Guide Note 10: Development of an Opinion of Market Value in the Aftermath of a Disaster relate to Market Value; Applicability of Basic Valuation Considerations; Principles, Sustainability of Value; and Competency Issues.

Guide Note 10 is intended to focus on market value assignments. As summarized directly from Guide Note 10, an appraiser must be especially mindful of the key components of the definition of market value when appraising in an unstable market that has been impacted by a disaster. Quite often, in the aftermath of a disaster, these key components of the definition of market value are absent from the transactions that occur – if any occur at all. For example, buyers and sellers might choose to act before they have full information. Because of the disaster, they might be extraordinarily motivated to buy or to sell. Exposure times for properties on the market might become extended, or might suddenly become contracted. Sometimes, market activity will virtually cease altogether in the aftermath of a disaster; open escrows fall out; prospective sellers cancel plans to sell; and prospective buyers cancel plans to buy. The lack of data only further exacerbates the challenge for the appraiser.

Further, Guide Note 10 reminds us that any appraisal problem must be approached using recognized appraisal methodology and in light of basic valuation principles, regardless of whether market conditions are at their most chaotic. Applying established approaches to solving valuation problems will help to simplify even the most complex assignments. Valuation in the aftermath of a disaster requires special attention to the fundamental appraisal principles of supply and demand, anticipation, change, substitution, contribution, externalities, and balance.

Any or all of the forces that influence real property values and the factors that create value might be impacted by a disaster. This is especially true with regard to residential real estate given the immediacy of addressing residential repairs and replacing adequate shelter. As a result, sharp increases in asking and selling prices might be observed. This raises several questions from an appraisal viewpoint: Do such higher prices represent "market value"? Are the parties to the transactions "typically motivated" and acting in their best interest or is their behavior irrational? Are the properties being exposed on the market for a "reasonable" length of time prior to sale?

The principles of substitution, contribution and externalities help provide the answers to these questions. In addition, the principles of anticipation and change are also especially relevant to valuation assignments in the aftermath of a disaster. While these fundamental principles provide a framework from which to appraise, the durability of the value conclusion in the aftermath of a disaster is also a key issue to address. Changes in market conditions may cause changes in market value to occur more rapidly than usual.

Further, Guide Note 10 reminds us of the requirements of the Appraisal Standard’s Competency Rule. This rule become greatly enhanced in assignments to develop market value opinions in the aftermath of a disaster.

The Appraisal Institute has significant resources available to its membership to assist in performing complex appraisal assignments for real property. The Guide Notes to the Standards of Professional Appraisal Practice are just one tool available to Appraisal Institute members, candidates, practicing affiliates and affiliates.

Bud Clarke, MAI, is the 2018 president of the Massachusetts and Rhode Island Chapter of the Appraisal Institute and senior vice president at Boston Financial Investment Management, LP, Boston, Mass.