The 50% FEMA Rule in The Hurricane Aftermath

After a hurricane or flood catastrophe, property owners with buildings located in flood zones not only deal with insurance adjusters and contractors, but also with their local building department. In many cases, the repair or rehab of a non-elevated structure will require a 50% FEMA Rule Appraisal. Building departments, tasked with the duty to abide by their municipality's flood ordinances in conjunction with the rules and guidelines established by FEMA, are often overwhelmed in a post disaster time, overrun by residents who want to do just one thing: repair their homes and move back in. Most often, residents are left with only sparse information, leading to permitting mistakes and disadvantages for the homeowner or association. This article gives an overview of FEMA rules and guidelines, why building departments have to abide by them and most importantly how property owners should approach the building permit application without disadvantaging themselves.

<u>FEMA and the National Flood Insurance Program</u>

Most people are familiar with the work that FEMA is most known for, namely serving the public during and after disasters with response, recovery and financial aid. In addition to this, FEMA is also the official source for flood hazard information in support of the National Flood Insurance Program (NFIP), which it administers.[1] The NFIP includes flood plain management regulations, which establish the minimum requirements for communities that must be met in order to comply with development regulations for new and existing structures in flood hazard areas.[2]

When buildings undergo repair or improvement, it is an opportunity for local floodplain management programs to reduce flood damage to existing structures. More than 21,000 communities participate in the National Flood Insurance Program (NFIP), which is

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[1] FEMA, "The National Flood Insurance Program," https://www.fema.gov/national-flood-insurance-program.
[2] Patricia Staebler, "The 50% FEMA Appraisal," The Appraisal Journal (Fall 2017): 264

managed by the Federal Emergency Management Agency (FEMA). To participate in the NFIP, communities must adopt and enforce regulations and codes that apply to new development in Special Flood Hazard Areas (SFHAs). Local floodplain management regulations and codes contain minimum NFIP requirements that apply not only to new structures, but also to existing structures which are "substantially improved (SI)" or "substantially damaged (SD)."[3]

Enforcing the SI/SD requirements is a very important part of a community's floodplain management responsibility. There are many factors that local officials will need to consider and several scenarios they may encounter while implementing the SI/SD requirements.[4] [5]

The Substantial Improvement/Substantial Damage Desk Reference provides municipalities with guidance on the minimum requirements of the NFIP regulations. Flood ordinances that are more restrictive supersede the guidelines, exceeding the NFIP minimums with e.g. freeboard. [6]

Most communities participate in the community rating system (CRS)[7], a voluntary incentive program that recognizes and encourages community floodplain management that complies with or even exceeds NFIP requirements. As a result, flood insurance premium rates are discounted in participating communities to reflect the reduced flood risk resulting from community actions.[8] The three goals of the CRS are:

- Reduce flood damage to insurable property
- Strengthen and support the insurance aspects of the NFIP

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3 ibid.
4 ibid.
5 Substantial Improvement/Substantial Damage Desk Reference
6 Freeboard is the voluntary addition of base flood elevation (BFE) to the BFE found in flood maps
7 FEMA, 'National Flood Insurance Program Community Rating System,' https://www.fema.gov/national-flood-insurance-program-community-rating-system.
8 Patricia Staebler, "The 50% FEMA Appraisal," The Appraisal Journal (Fall 2017): 264

- Encourage a comprehensive approach to floodplain management

Municipalities have ample motivation to utilize the 50% FEMA rule as basis for compliance with FEMA rules and regulations, because communities that do not comply must take into consideration that there is a high likelihood the insurance risk rating for the NFIP could increase, thus affecting the entire community, and every property owner. [9]

It is important to recognize that municipalities write their own, unique flood ordinances. The rules implemented by cities or counties can be more stringent than FEMA requires, or in some cases, less stringent. It seems most municipalities interpret FEMA guidelines differently regarding improvements – some allow property rehab/remodel up to 50% only once in the lifetime of a property, some allow 50% every ten years, some allow 50% every ten years with the oldest year dropping out of the equation and so forth.[10]

There are different flood zones in which the 50% FEMA rule appraisal is needed: Zone A, AE, A 1-30, AH, AO, V, VE, V 1-30. The V flood zones differ from the A zones in that they have added high velocity wind risk and wave load. [11] Together with the base flood elevation (BFE), the Flood Insurance Rate Map (FIRM) regulates how a structure can be built or rebuilt in these zones. BFEs, which are the regulatory requirement for the elevation or flood-proofing of structures, are shown on FIRMs and on the flood profiles. [12] Figure 1 illustrates the base flood elevation and different levels of flood zones.

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[9] ibid.
[10] ibid.
[11] FEMA, "Flood Zones," http://www.fema.gov/flood-zones.
[12] Patricia Staebler, "The 50% FEMA Appraisal," The Appraisal Journal (Fall 2017): 263

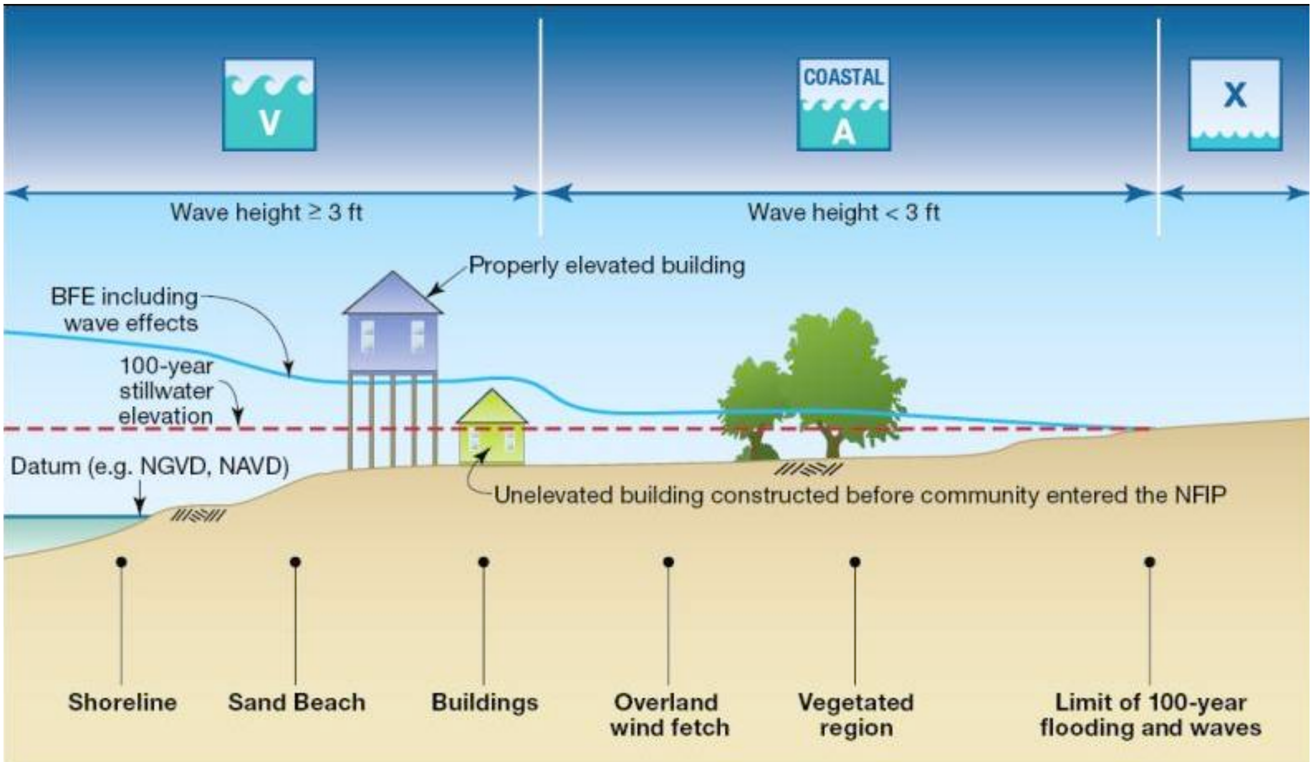

Figure 1[13]

The 50% FEMA rule appraisal is a tool that is used mostly in coastal areas, but overall for properties that are located in flood zones and subject to flood plain management. It gives the property owner an understanding of how much money they are allowed to spend to improve their property without triggering FEMA compliance, resulting in the requirement to elevate the property in order to bring it up to FEMA standards.

Communities must require that all new construction and substantial improvements of residential and commercial structures within Zones A1-30, AE and AH Zones on the community's FIRM have the lowest floor (including basement) elevated to

[13] FEMA, "Region II Coastal Analysis and Mapping," http://www.region2coastal.com/resources/coastal-mapping-basics/.

or above the BFE. Common elevation techniques include elevation on file (Flood Elevation Certificate), elevation on piles, piers or columns.[14]

All new construction and substantial improvements in Zones V1-30, VE, and also Zone V (if BFE data is available), must be elevated exclusively on pilings and columns, so that the bottom of the lowest horizontal structural member of the lowest floor (excluding the pilings or columns) is elevated to or above the BFE.[15]

The 50% FEMA rule states:

If the cost of improvements or the cost to repair exceeds 50% of the depreciated value of the structure, the property must be brought up to current floodplain management standards.[16]

$$\frac{\textbf{Cost of repair/renovation/addition}}{\textbf{Depreciated market value of the structure}} \quad \mathbf{>50\%}$$

If the cost of the project exceeds 50% of the building's value, it is a substantial improvement, which must meet floodplain regulations. The project needs to be adjusted to meet the 50% rule or the property will need to be brought up to code, which could mean elevation of the property to meet FEMA standards.

Affected projects can be those voluntarily undertaken or ones that are necessary after a catastrophe (e.g. wind, flood, fire, etc.):

- Remodeling
- Rehabilitation
- Building Additions
- Repair
- Reconstruction (partial)

[14] Patricia Staebler, "The 50% FEMA Appraisal," The Appraisal Journal (Fall 2017): 265
[15] ibid.
[16] Substantial Improvement and Substantial Damage Desk Reference FEMA P-758 / May 2010, Chapter 4

Part 2

Based on the FEMA “Substantial Improvement and Substantial Damage Desk Reference”, there are four different ways to determine the depreciated value of a property for the 50% FEMA rule appraisal:

1. Professional Property Appraisal
2. Adjusted Assessed Value
3. Qualified Estimates
4. Actual Cash Value

1. **The Professional Property Appraisal** refers to the “every day” market valuation based on sales comparables, while deducting the land and every site improvement, such as pools, detached structures, etc. The market value can be too low in many cases, especially when the property is located on a parcel of land with a high land value. The lot the property sits on cannot be included in the 50% FEMA Rule Appraisal. and deducting the land from the market value most often results in too low a value. [17]

2. **The Assessed Value** is based on the property appraiser or assessor’s value and is even lower than the market value. Assessed value will be detrimental for the property owner, especially when dealing with condominium property. [18]

3. **Qualified Estimates** are developed by a “qualified official” of the building department, which places the impartiality of such an estimate into question. Qualified estimates can be based on “recent permit records, recent home sales, regional cost data, estimates of depreciation based on knowledge of the pre-damage condition of buildings, and adjustments for unique or distinctive features

[17] FEMA, Substantial Improvement/Substantial Damage Desk Reference, 4.5.1.
[18] FEMA, Substantial Improvement/Substantial Damage Desk Reference, 4.5.2.

of individual buildings." [19]

4. Actual Cash Value is the fourth method for the 50% FEMA rule appraisal, and in my opinion, the only valid valuation, because this method:

- Estimates the cost of construction "as-built"
- Allows for proper application of depreciation
- Does not consider land value
- Does not include any site improvements
- Is easy to understand by construction professionals, building contractors and building officials alike[20]

"Actual cash value (ACV) is the cost to replace[21] a building on the same parcel with a new building of like-kind and quality, minus depreciation due to age, use, and neglect. ACV does not consider loss in value simply due to outmoded design or location factors. The concept of ACV is used in both the insurance industry and the construction industry. In most situations, ACV is a reasonable approximation of market value. Depreciation accounts for the physical condition of a structure. Depreciation does not take into account functional obsolescence (e.g., outmoded design or construction that pre-dates current codes) or factors that are external to the structure (e.g., reputation of schools or distance to shopping and parks). Commercially available references provide tables and formulas to calculate physical depreciation. These tables and formulas are objective and are used by most professionals in the fields of property appraisal and building inspection."[22]

Replacement Cash Value (RCV) minus depreciation results in Actual Cash Value (ACV).

[19] Substantial Improvement and Substantial Damage Desk Reference FEMA P-758 / May 2010
[20] FEMA, Substantial Improvement/Substantial Damage Desk Reference, 4.5.3.
[21] Here, cost to replace has the same meaning as replacement cost.
[22] Substantial Improvement and Substantial Damage Desk Reference FEMA P-758 / May 2010 4.5.3.

The following items can be included in the 50% FEMA appraisal: [23] [24]

All structural elements, including:

- Foundation
- Slabs
- Bearing walls, tie beams and trusses
- Floors and ceilings
- Attached decks and porches
- Interior partition walls
- Exterior wall finishes (brick, stucco, siding) including painting and moldings
- Windows and doors
- Hardware

All interior finishing elements, including:

- Floor finishes
- Bathroom cabinets and fixtures
- Wall and ceiling finishes
- Kitchen cabinets and fixtures
- Built-in bookcases, cabinets, and furniture
- Hardware

All utility and service equipment, including:

- HVAC equipment
- Plumbing and electrical services

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[23] FEMA, 'Floodplain Management Requirements,' https://www.fema.gov/floodplain-management-requirements, 283.

[24] Please note that both the list of what can and what cannot be included is based on the FEMA handbook "Substantial Improvement and Substantial Damage Desk Reference FEMA P-758 / May 2010.

- Light fixtures and ceiling fans
- Security systems
- Built-in kitchen appliances
- Central vacuum systems
- Water filtration, conditioning, or recirculation systems

And last but not least:

- Overhead and profit

The following items cannot be included:

- Plans and specifications
- Survey costs
- Permit fees
- Post-storm debris removal and clean up
- Landscaping
- Sidewalks
- Fences
- Yard lights
- Swimming pools
- Screened pool enclosures
- Detached structures (including garages, sheds and gazebos)
- Landscape irrigation and lighting systems

So how should property owners approach the repair/rehab/reconstruction of their property?

- Hire a contractor to estimate the amount for the planned project
- Contact the building department to evaluate if a 50% FEMA appraisal will be necessary for the planned project; do not apply for a permit yet
- If an appraisal is needed, hire an appraiser to prepare a 50% FEMA rule appraisal to evaluate the depreciated market value of the property
- Apply the formula as shown above
- Determine if the property meets the 50% FEMA rule
- If yes, go ahead and apply for a permit
- If no, there are two ways to go:
    - Adjust the project cost
    - Decide to bring the property up to code

How should a condominium association handle the permitting process?
It depends on what kind of property we are dealing with; here are some examples:

<u>Condo Associations with multiple similar villas:</u>
Instead of getting an appraisal for all affected villas, the appraiser should evaluate the buildings with the largest amount of damage. If the villas are all of the same size, one appraisal might be sufficient. If there are several floor plans with varying sizes, each floor plan should have one separate appraisal.

<u>Condo Associations with villas, duplexes, four-plexes:</u>
For every type of building the one with the largest amount of damage should be evaluated. Also, in this case, every different affected building type needs a separate appraisal. If there are different floor plans for each building type, they will need a separate appraisal report as well.

Condo Associations with mid- and high-rises:

The larger the building, the more the likelihood that the requirements for the 50% FEMA Rule will be met. The damage to mid- and high-rises can usually be easily covered by the total value of the property. Keep in mind, however, that the size of the building does not prevent the application of the FEMA rule. Condos are especially difficult for building departments to estimate, because the property appraiser only displays the values of the individual condo units. The sum of all condo unit values might not be sufficient to meet the FEMA requirements.

In any case, it is vital to work with professionals to determine the best way to accomplish your communities' goals when it comes to rehabbing buildings in flood zones. If you hire an appraiser they will be advocating for you. An appraiser, like an attorney, is bound by confidentiality and loyalty to their client.

Also, if you get a settlement from your insurance company, do not use the line item estimate from your adjuster as basis for the building permit. The adjuster's calculation might contain items like debris removal or clean-up which do not have to be counted under the FEMA guidelines.

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