UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE

In re: Bk. No. 00-10641-JMD
Chapter 13

Stergios Manakos and
Voula Manakos,
Debtors

Stergios Manakos and
Voula Manakos,
Plaintiffs

v. Adv. No. 00-1067-JMD

BCC Investors, L.L.C.,
Defendant

MEMORANDUM OPINION

I. INTRODUCTION

In this adversary proceeding the Debtors are seeking a determination of the extent of the secured claim of BCC Investors, L.L.C. (the "Defendant") pursuant to 11 U.S.C. § 506 (a).[1] The parties agree that the Defendant's second mortgage on the Debtors' personal residence is only partially secured and that because the Defendant holds other collateral securing the Debtors' obligations to it, the Defendant's secured claim may be modified by the Debtors' Chapter 13 plan pursuant to § 1322(b)(2).

This Court has jurisdiction of the subject matter and the parties pursuant to 28 U.S.C. §§ 1334 and 157(a) and the "Standing Order of Referral of Title 11 Proceedings to the United States Bankruptcy Court for the District of New Hampshire," dated January 18, 1994 (DiClerico, C.J.). This is a core proceeding in accordance with 28 U.S.C. § 157(b).

II. FACTS

[1] Unless otherwise noted, all section references hereinafter are to Title 11 of the United States Code.

The parties have stipulated to all of the material facts in this case with the exception of the reasonable value of the Debtors' personal residence.[2] The Debtors own a personal residence located at 10 Robin Road, Concord, New Hampshire (the "Property"). On the petition date the Property was subject to a first mortgage in favor of Citicorp Mortgage, Inc. securing an obligation in the amount $52,609.79. The Debtors and Photias N. Tsantoulas are obligated to the Defendant under the terms of a promissory note dated August 31, 1988 in the amount of $153,778.72 (the "Note"). The Note is also secured by real property owned by Mr. Tsantoulas, the third maker of the Note. The Debtors contend that the reasonable value of the Property is $89,000.00 and the Defendant contends that the reasonable value of the Property is $112,000.00.

Each party presented testimony by an expert residential appraiser supporting their respective views on the value of the Property. The appraisers utilized substantially similar techniques and standards. Both appraisers had meaningful professional credentials, significant experience in appraising residential real estate, and knowledge of the market and the Property. Both appraisers were credible witnesses.

The Debtors presented the testimony of Louis C. Manias. Mr. Manias testified that the Property was a twenty-four year old modular home similar in construction and quality to other modular homes of that age in the greater Concord area. A modular home is constructed in an offsite location, typically a factory, and transported to the site in two sections. These sections are then placed on a foundation and bolted together. The exterior siding is then applied with the result that from the exterior the modular home looks similar to a "stick built" home. Mr. Manias testified that the Property was of average quality and in average condition for similar homes in the Concord area. He noted that while the interior of the Property was well maintained, several conditions on the exterior of the Property adversely impacted the value of the Property.

Mr. Manias testified that he identified several adverse conditions on the Property which a potential buyer would discover upon inspection of the Property. He testified that a buyer would either require these

---

[2] The parties stipulated at the commencement of the trial that the interest rate to be charged is a matter to be addressed at confirmation.

conditions to be cured prior to closing or would insist upon price concessions from the seller. Mr. Manias testified that while inspecting the roof he noted that "hundreds" of staples used to affix the shingles to the structure were popping up, indicating that the roof was near the end of its useful life. He testified that this condition would be obvious to any home inspector and would impact the price that a buyer would pay. Based upon discussions with third party contractors, Mr. Manias estimated the cost of replacing the roof at $4,000.00. He also noted several holes in the soffit and fascia boards where the roof and the outside walls meet. He determined that the holes were due to squirrels entering the Property and living in the attic. Although the critter problem had been solved, he stated that the soffit and fascia were constructed from Masonite, a wood substitute used in other modular homes of similar age, but not in similar stick built homes or current modular homes. He testified that a buyer would want the holes fixed and surfaces replaced with wood. Based upon conversations with third party contractors, Mr. Manias estimated the cost to replace and repair the soffit and fascia boards at $5,000.00. Further, he testified that while inspecting the foam insulation surrounding the outside of the foundation he noted possible insect infestation which he confirmed as termites through conversations with a pest control contractor. The cost to eliminate the termites was estimated at $1,500.00. In summary, Mr. Manias testified that the cost of remedying these three conditions would be, in the aggregate, $10,500.00. Accordingly, he made a downward adjustment in that amount in reaching the final value of $89,000.00 in his appraisal. See Exhibit 1.

The Defendant presented the testimony of Mr. Peter Stanhope. Mr. Stanhope testified that a separate adjustment to the value of the Property due to its construction as a modular home versus a stick built home was not warranted for the submarket that includes the Property (i.e., the entry level affordable housing market). He testified that the current market was very active with an insufficient supply of lower cost housing to meet the demand. Accordingly, Mr. Stanhope concluded that the market would not discount solely for the fact of modular construction, but that the overall condition of the property was the most important factor. He testified that no separate adjustment for the condition of the roof was warranted because there was no evidence of roof failure on interior ceilings (i.e. stains or water damage) and that the adjustment of comparable sales for buildings of similar age or older would account for any increased maintenance issues in an older structure. In effect, Mr. Stanhope felt that adjusting for condition and the cost of a new roof would be duplicate adjustments. He testified that the squirrel problem had been solved by the Debtors' installation of wire mesh or metal to seal entry holes for animals. While further minor repairs might be necessary, Mr. Stanhope testified that replacement of the soffit and fascia boards would not be necessary to market the Property. Finally, Mr. Stanhope testified that he had not observed any termite infestation or damage and, accordingly, had not adjusted for any pest eradication or treatment expense. After making adjustments to the values of comparable sales to account for differences between them and the Property, Mr. Stanhope arrived at a final value of $112,000.00 in his appraisal. See Exhibit 101.

III. DISCUSSION

The appraisers for the parties to this proceeding used the same standard method for valuing residential real estate, the sales comparison approach, yet reached results which are nearly twenty-six percent, or $23,000.00 apart. This difference is significantly greater than would be expected from two residential appraisals on an entry level residence conducted by two experienced professionals. Because both appraisers determined their final values based primarily on the sales comparison approach, but utilized the cost approach to support their respective conclusions, the Court shall first examine their cost approach analysis to determine whether any significant differences exist between the appraisers' views of the Property itself.

A. COST APPROACH VALUATION

An examination of the cost approach section of each appraisal report reveals that the Debtors' appraiser valued the replacement cost of the improvements to the Property at $93,887.00 while the Defendant's appraiser valued the improvements at $88,806.00, a difference of slightly less than ten percent. This difference would be more in line with the maximum variance to be expected from two professional appraisers in a residential appraisal for an entry level residence. Although the Property is a twenty-four year old modular home, the Debtors' appraiser determined that its economic life, or age, was fifteen years while the Defendant's appraiser determined the economic life was eleven years. Consequently, the Debtors' appraiser depreciated his replacement cost estimate by a significantly greater amount than the depreciation used by the Defendant's appraiser.[3] Despite the fact that the Debtors' appraiser started with a higher cost for the improvements to the Property, the Defendant's depreciated cost approach value of $108,800.00 was nearly sixteen percent higher than the Debtors' depreciated cost approach value of $93,887.00.

Based upon the testimony at trial, it appears to the Court that the major difference of opinion between the appraisers regarding the "economic age" of the Property, for purposes of depreciated cost value and comparison sales adjustments, is based upon their views on the quality of materials and construction used in modular homes at the time the Property was built, and the impact of those perceptions on the market. The Debtors' appraiser testified that the roof was stapled on to the structure instead of being nailed, an inferior construction in his opinion, and that "hundreds" of staples were visibly lifting up from the roof itself. In addition, he testified that the soffit, fascia boards and siding were Masonite rather than wood. In his opinion, Masonite is inferior to wood over a prolonged period of time and is not comparable to "stick built" homes similar in age to the Property. The Defendant's appraiser testified that he did not observe any problems with either the exterior of the roof or any evidence of staining or leaks on the interior ceilings of the Property. In addition, he testified that based upon an internal study by his firm, he has not observed that the market applies any discount for older modular homes compared to stick built homes similar to the Property in the Concord area.

The Court believes that the difference of opinion between the appraisers over the discount, if any, applied by the market, in valuing modular versus stick built homes of comparable age, to the Property is the primary reason for their differences in the depreciated cost value of the Property. In addition, the Court

[3] The Debtors' appraiser estimated physical depreciation at $23,129.00 and functional depreciation at $10,500.00 for total depreciation of $33,629.00. The Defendant's appraiser estimated physical depreciation at $9,769.00 and functional depreciation at $3,275.00 for total depreciation of $13,044.00.

believes that this same difference in opinion has impacted their estimate of the "quality of construction" factor in the adjustment of the value of comparable sales in their respective sales comparison analyses. While the Court believes that Masonite may not age as well as wood on the exterior of a structure, the evidence presented at trial does not compel a conclusion in either direction. The Debtors' appraiser based his opinion on his experience and observations in the market. The Defendant's appraiser based his opinion on empirical data developed by his firm. However, neither appraiser presented any specific evidence to support their conclusions. The absence of any testimony on the factual basis for their conclusions prevented the opposing party from testing the conclusion of the other party's appraiser. In fact, it is possible that both appraisers may be correct. Masonite may not age as well as exterior wood siding, but in homes of similar age and condition, the market may not currently be discounting for this factor due to the tight supply of entry level housing.

B. COMPARISON SALES VALUATION

Both appraisers utilized the comparison sales approach to determine their respective opinions of value. The major differences in the comparison sales approach used by each appraiser appears to involve three areas: (1) a downward five percent quality of construction adjustment by the Debtors' appraiser for the use of Masonite on exterior surfaces and smaller than normal floor joists; (2) a downward functional utility adjustment of $10,500.00 for the estimated cost to remedy an apparent termite infestation ($1,500.00), replace the roof ($4,000.00), and replace the Masonite soffit and fascia boards with wood to correct the damage caused by a previous squirrel problem ($5,000.00); and (3) the Defendant's use of comparison sales that had greater area and privacy than the Property. The Court will consider each of these differences and the record developed by the parties at trial.

The Defendant's appraiser testified that the five percent reduction for quality differences between older modular construction and stick built homes applied by the Debtors' appraiser was not justified by the market data for home sales in the Concord area. Without presenting the Court with evidence of the aforementioned data, the Defendant's appraiser testified that, due to current market conditions in Concord, modular homes were able to compete favorably with stick built homes. The Defendant's expert further testified that the five percent reduction was duplicative of the functional utility adjustment also applied by the Debtors' appraiser. Based upon the testimony at trial, the Court concludes that the Debtors' appraiser has, in part, factored his views on the modular versus stick built difference into both adjustments. For the reasons set forth above, the testimony of the appraisers regarding the issue of a market discount for older modular homes quality of construction was not adequately justified by either appraiser. Accordingly, the Court finds that the Debtors have not justified a five percent quality of construction adjustment.

Unlike the quality of construction adjustment, the functional utility adjustment applied by the Debtors' appraiser was based upon actual observed conditions and his consultation with area contractors regarding the cost to correct the identified deficiencies. The Debtors' appraiser testified that the termite infestation evidence discovered in his inspection would need to be remedied prior to any closing. In addition, he testified that an inspection of the roof, from the level of the roof itself rather than from ground level, would reveal the extent of the roof problem and would either lead to price concessions by a seller or a correction prior to a sale. The Defendant's appraiser did not observe any evidence of termite infestation and only looked at the roof from the ground. With respect to the cost of replacing the soffit and fascia boards, the Defendant's appraiser testified that repairs had already been made, a few more minor repairs would fully take care of the problem, and that replacement would not be necessary. The Court finds that replacement of some exterior trim would likely be required for any sale to a third party, but that replacement of all soffit and fascia boards was not justified by the testimony. Accordingly, the Court finds that the functional utility adjustments applied by the Debtors' appraiser for the termite infestation ($1,500.00) and the roof ($4,000.00) were justified by the evidence while an adjustment for repair of the soffit and fascia boards ($5,000.00) was not justified. However, the Court will include an adjustment of $1,500.00 for minor repairs. Accordingly, the functional utility adjustment will be reduced from $10,500.00 to $7,000.00, or a reduction of $3,500.00.

The Defendant's appraiser provided three comparable sales, but gave the most weight to comparable sales number one and two. The Property consists of 0.32 acres on a residential street with neighboring houses on both sides. Comparable sale number one is a wooded site of 0.62 acres with underground utilities and greater privacy than the Property. See Exhibit 6. Comparable sale number two is also a wooded, well landscaped lot of 0.57 acres. The Defendant's appraisal report stated that "[a]ll comps are adjusted for the greater utility & privacy afforded by their larger site areas." See Exhibit 101 at page 2. However, the actual adjustment for each of these two comparable sales was $1,000.00. In his cost analysis, the Defendant's appraiser cited a sale of a 0.32 acre lot on Penacook Street in Concord in January 2000 as his basis for computing the value of the Property's site as of the date of his appraisal. When asked by the Court to explain his adjustment to the comparable sales for differences in the size and privacy of those sites compared to the Property, he testified that the market did not make significant adjustments for such factors as long as the site was a building lot with similar utility services. The Court finds lacking the rationale for the de minimis (1.0%) adjustment for differences in the sites of comparable sales number one and two versus the site of the Property. Even in the current seller's market for residential real estate, the Court finds that the a building lot which is nearly twice as big, affords greater privacy, and has underground utilities would sell at a premium over a smaller lot with less privacy and above-ground utilities. If the value of the smaller building lot, as determined by the Defendant's appraiser, is $28,000.00, then the larger lot would appear to have a greater value than $1,000.00 more, or $29,000.00. If the values of two building lots are significantly different, then the Court believes that most, if not all, of that difference would be reflected in the value of an improved building lot, so long as the improvements are comparable in quality and extent to other similar properties in the community. In the absence of any testimony on this issue the Court must either not consider the comparable sales used by the Defendant's appraiser or make an adjustment. The Court elects to apply a differential of fifteen percent to the value of the site for the Property, rather than the

$1,000.00 adjustment utilized by the Defendant's appraiser, in order to adjust for site differences. Accordingly, the Court will decrease the sales comparison value by $3,200.00.[4]

In consideration of the adjustments discussed above, the Court has recalculated the fair value of the Property, as determined by each appraiser as follows:

Debtors' Appraiser:	
Appraiser's Valuation	$ 89,000.00
Add back adjustment for quality of construction (5.0%)	+$ 4,450.00
Reduction in functional utility adjustment	+ $ 3,500.00
Adjusted Fair Value	$ 96,950.00
Defendant's Appraisal:	
Appraiser's Valuation	$112,000.00
Adjustment for site differences	- $ 3,200.00
Adjusted Fair Value	$108,800.00

After the adjustment of each appraiser's valuation for the differences identified in the testimony at trial, the difference in value between the two appraisal experts (12.2%) remains slightly greater than what might be expected. In view of the size of the difference in values, the similar qualifications and credibility of each appraiser, and the nature of the Property, the Court will resolve the differences in this case by giving equal weight to the above adjusted fair values. Therefore, the Court determines that based upon the appraisal testimony, other evidence presented at trial and the reasons set forth above, the value of the Property is at the midpoint between the adjusted fair values, or $102,875.00. Accordingly, the value of the Defendant's secured claim is equal to the value of the Property ($102,875.00) less the amount of the first mortgage ($52,609.79), or $50,265.21, and the value of its unsecured claim is the amount due on the Note ($153,778.72) less the amount of the secured claim ($50,265.21), or $103,513.51.

IV. CONCLUSION

For the reasons set forth above, the Court determines that the value of the Defendant's secured claim is $50,265.21 and the value of its unsecured claim is $103,513.51. This opinion constitutes the

---

[4] The difference between fifteen percent of the site value determined by the Defendant's appraiser ($28,000.00 x 0.15 = $4,200.00) and the site adjustment utilized by the appraiser ($1,000.00).

Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. The Court will issue a separate judgment consistent with this opinion.

DATED this 8th day of September, 2000, at Manchester, New Hampshire.

J. Michael Deasy
Bankruptcy Judge