

CHAPTER 17

FINANCING LAND DEVELOPMENT PROJECTS

Chapter Objectives

- Project Development
vs.
Land Development
- Option Contracts
- Lender Requirements
- Holdbacks
- Release price

Development Decision

- 1. A site looking for a use
 - Often public sector authorities are involved
- 2. A use looking for a site
 - Mostly large development firms
 - Retail business expansion

Types of Building Construction

- Build to suit
 - Usually a long term lease arrangement
- Turnkey basis

Land Development Process *Stage One*

Often, the land development process begins with a negotiation of an option agreement. These are non-refundable

Stage 1:

- Site inspection
- Preliminary market study
- Preliminary cost estimates

Land Development Process *Stage Two*

Stage 2:

- Soil Studies, Engineering
 - Excavating, topography, grading, subsurface characteristics
- Feasibility, Appraisal, and Design Strategy
- Bidding: negotiating with contractors
- Submit plan for public approvals
- Submit package for financing

Land Development Process *Stage Three*

Stage 3:

- Purchase land
- Close on architecture and design loan
- Begin construction of improvements
 - Surface improvements, utilities
- Implement financial controls
- Coordinate with contractors, and consultants, public sector

Land Development Process *Stage Four*

Stage 4:

- Implement marketing program
- Additional coordination with builder
- Implement design controls with builders
- Implement facility management, Homeowners Associations, or other management entity (in NYC, this could be a co-op board)

Use of the Option Contract

- The lowest price possible for the longest period of time
- Ties up the land = **Time**
- Precludes the landowner from selling the land
- 1 Month to 3 Years
- Stage 1 and Stage 2 of land development process
- As opposed to a contract, this money is typically non-refundable.

Financing and Development

- Purchase for cash
- Down payment with seller financing (purchase money mortgage)
- Seller must subordinate to construction loan
- Partial release clause in mortgage

Financing and Development Continued

- A & D loan to finance land and improvements
- Floating rate loans- Prime plus 2% to 3%
- “Draws”
- Lender requirements are much the same as project financing

General Contracts and Subcontracts

- Lenders prefer fixed price contracts
- Completion bonds
- Title insurance
- Holdbacks or retentions (10%)
- Extension agreements (if developer needs more time, it's built into mortgage agreement for a fee)

Estimating Development Cost and Interest Carry

- Land Acquisition and Development costs
- Operating Expenses
- Draws and Revenue Estimates
- Sales and Repayment Rates
- Release Schedule

Estimating Development Cost and Interest Carry

LAND COST		\$2,400,000
DEVELOPMENT COST		
Hard costs		
Grading/clearing	\$390,000	
Paving	\$540,000	
Storm sewers	\$70,000	
Sanitary sewers	\$125,000	
Water	\$125,000	

Estimating Development Cost and Interest Carry Continued

Electricity	\$120,000	
Landscaping	\$90,000	
Other	\$90,000	
Amenities	\$390,000	
Subtotal		\$1,940,000

Estimating Development Cost and Interest Carry Continued

SOFT COSTS		
Engineering	\$110,000	
Direct overhead	\$80,000	
Public approvals, tap fees, etc.	\$90,000	
Miscellaneous direct costs	\$80,000	
Legal and accounting fees	\$100,000	
Contingencies	\$240,000	
Construction interest	\$451,052	
Construction loan fees	\$122,732	
Subtotal- soft costs		\$1,273,783
Total land, hard and soft costs		\$5,613,783

Estimating Development Cost and Interest Carry Continued

OPERATING EXPENSES		
Selling commissions	\$342,000	
Property taxes	\$87,500	
General and administrative	\$210,000	
Marketing costs	\$100,000	
Total operating expenses		\$739,500
Total project cost		\$6,353,283

Land and Development Other Conditions

- Revenue estimates
- Absorption rate
- Construction draws
- Sales and repayment dates

Land and Development Other Conditions Continued

- Release schedule
- Repayment schedule
- Project feasibility and profitability
- IRR and NPV

Developers Cash Flow

	Cash Inflows	Cash Outflows
0	\$1,019,200	\$2,642,843
1	\$2,016,204	\$2,042,454
2	\$1,138,517	\$1,078,896
3	\$881,366	\$734,612
4	\$867,174	\$764,169
5	\$1,486,285	\$1,198,096
6	\$1,456,987	\$1,168,798
7	\$1,036,375	\$688,194
8	\$1,026,375	\$121,300

□ Cash inflows include construction draws, interest draws and sales

□ Cash outflows include direct and indirect cost of construction

Net Cash Flow

0	-\$1,622,643
1	-\$26,250
2	\$59,621
3	\$146,755
4	\$10,300
5	\$288,189
6	\$288,189
7	\$348,182
8	\$904,700
IRR = 16.64%	
NPV = \$41,558	