

# Evaluating A Land Note

by Stanley Gainsforth

*The joker*

in the paper deck of cards is the land note.

A house is a house. The houses in any one area are more or less alike, and they have sold in a narrow range. A commercial property is a commercial property, with values based on income: If the income from the property won't make the payment on the loan, don't buy the loan! But there are no such guidelines on a land loan.

An appraiser can make mistakes, but its very rare for an appraiser to estimate the value of a property as **DOUBLE** or **TRIPLE** or even **FIVE TIMES** the real value. But it can happen on a land loan!

How is that possible? Land has a unique characteristic that determines its value: There is nothing built on land. Therefore, research is required to determine what, if anything, can be built on it. If it is possible and legal to build a house on the land, it is worth a lot more than if it is not. **Land can be worthless!**

Here are some of the questions to ask when evaluating a land note:

- Does the land have water, power or sewer available? What are the costs to hook up? Is it practical to do so?
- Does it have legal access? A "road that does not show on public records may not be legal, or it may require court action or negotiation with other owners to legally validate it.
- Does the land qualify for construction under the guidelines as set down by the governing authority for construction in the area? Examples:
  - A. Does not meet minimum lot size requirement.
  - B. Does not perk for septic.
  - C. Not geologically stable for construction.
  - D. Subject to other requirements for approval of construction that would make it impractical, such as a street-widening action that would reduce the size of the

lot, or a large assessment of some kind that would have to be paid before construction could begin.

Is the zoning determined and correct? In some cases, large tracts of land are subject to building moratoriums where local governments want to discourage growth.

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If the land is within five miles of the Pacific coast of California, it falls under the auspices of the Coastal Commission, a body that has historically been unwilling to approve construction.

Are there special environmental concerns? It may be necessary to pay for an environmental impact study, a geology report, coastal commission approval, a percolation test and a confirmation of zoning to even determine whether it may be legal and practical to build on a piece of land. In other cases, it may be necessary to spend a lot of money meeting the requirements of governing bodies before construction can begin.

This does not mean I am shy about land notes. They can be excellent. Interest rates are higher, the notes are usually first liens, loan-to-value ratios are lower and it may be possible to see that the land is buildable and valuable by virtue of building around it or a history of approvals in the area.

But land parcels should be appraised by someone competent in the area, and brokers and investors should be wary of "lizards and cactus" parcels or parcels in areas where there have been problems in development in the past.

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