

23 DEVELOPERS OF LAND AND BUILDINGS

The development of real estate provides a portion of the inventory that a real estate broker utilizes in his or her business. Just as any retailer or wholesaler must stock adequate inventories of their products, the real estate broker stocks listings of real property. The broker constantly replaces sold or expired listings with new listings, some of which may come from developers in the form of “new homes or lots.”

Real estate developers usually function in a larger business “arena” than do real estate brokers. Developers “manufacture” residential, commercial or industrial sites, either as vacant lot subdivisions or as improved or partially improved subdivisions. Their goal is to supply the type and price range of product that will satisfy the market.

In the course of business, a developer often:

- carries inventory of raw land, semi-finished and/or finished products, often for lengthy periods and for several widely separated, ongoing projects both “spec” (for sale) and custom (pre-sold);
- uses personal funds or negotiates loans from land sellers, joint venture partners (private investors) or financial institutions; and
- assumes large risks because of land planning uncertainties and possible misjudgment of the market which result in delays and losses due to interest payments, carrying charges, overhead, and other costs.

Some developers specialize in converting raw land to finished lots, suitable for builders to buy and begin construction of off-site as well as on-site improvements. Often the land developer will also install the principal off-site improvements and infrastructure (roads and utilities). Other developer-builders plan and complete the entire subdivision from raw land through construction and sale of homes. Developers can be national, regional or local and many parts of California have historically had some or all to varying degrees. Developers tend to be very entrepreneurial and usually are very market anticipatory. Interestingly, there are no state requirements such as licensing for developers or subdividers.

SUBDIVIDING

A subdivider builder or developer must understand the potential difficulties involved in subdividing and the market for the project. The development plan must take into account state and local government regulation (e.g., the Subdivided Lands Law, the Subdivision Map Act, the California Environmental Quality Act, zoning, local general and specific plans and the effects of public opinion to the development).

Often, zoning and planning preconditions drastically reduce the potential of a property. Before a developer or builder purchases property, he or she should consult with the local planning agency and private land use specialists to evaluate the likelihood of final approval of a project and the probable time frames for accomplishing the approval process.

A developer will use civil engineers, construction engineers, soil engineers, land use planners, building architects, landscape architects, contractors, attorneys, title companies, bankers, real estate analysts, market researchers, and cost accountants to formulate a plan consisting of the following:

1. physical layout of tract in engineered detail;
2. land use processing and approval schedule;
3. amenities to be provided;
4. initial financing and continuing financing until the last sale;
5. advertising and sales promotion.

To determine if the project will yield adequate profit, the developer must calculate:

1. cost of the land;
2. cost of government fees;

3. cost of off-site improvements (e.g., water mains, sewers, streets, gutters, curbs, sidewalks, and street lighting);
4. survey, legal, marketing, financing and office/overhead costs; and,
5. the likely retail sales price(s) of the lots or units sometimes far into the future.

The developer's educated guess at the rate at which the lots will sell (the absorption rate) will impact the marketing, financing, and overhead costs, all adjusted for anticipated future price fluctuations.

The sum of all costs and expenses of the project is subtracted from the estimate of the retail sales price of the lots to derive the estimated (pre-tax) profit along with factoring in the amount of time before profits will actually be realized.

A developer may subdivide a large tract of land pursuant to a phased master plan designed to meet the anticipated demand/absorption rate. These projects are more complex, with master governing restrictions and more obstacles to state and local approval and generally take more time and therefore more uncertainty.

A broker may gain initial experience in subdividing by becoming involved in a more limited aspect of the process. An owner of acreage might engage the broker as a subdivider, with the broker arranging the services of skilled consultants (civil engineer, land planner, land use attorney, etc.) to accomplish subdivision of the land. The broker and land owner may form a partnership: one contributing capital and land, the other management and marketing (sweat equity).

DEVELOPER-BUILDER

Development and building requires financing for land acquisition, land use approval and subdividing, construction, marketing, and carrying of inventoried properties financially until they are sold. A developer-builder often finds it desirable to set up specialized subsidiary companies with separate financing needs: one company to hold title and subdivide the property; another to conduct building operations; and another for sales and marketing.

Subdividing and building is a cyclical business. High productivity and profit may be followed by a period of depressed sales and losses. The cost of land, unpredictability of land use approvals, credit availability, interest rates, inflation, and changing property values are all important factors.

Developers must find ways to build affordable homes despite increases in:

- demands from local agencies as conditions for approval of projects;
- wages;
- cost of building supplies;
- energy conservation and other building code requirements;
- aggressive competition;
- insurance costs;
- some cost-saving options often considered are:
 - precut or prefabricated materials;
 - use of fewer skilled craftsmen through standardization of jobs;
 - complete on-site assembly of prefabricated units; and,
 - reduction of land cost per home through increased density (e.g., planned development/cluster home and condominium projects).

Even though production efficiency has increased, total construction costs have risen with inflation and the demands of the consumer for more amenities.

Furthermore, a potential home builder needs to be aware of the risk that defective construction can lead to legal claims from purchasers. This liability can endure for up to and possibly beyond ten years after the home is completed and has been an increasing critical issue over the last two decades.

HOME CONSTRUCTION

The details of home construction methods, special installations, price and quality of materials are not generally within the scope of the real estate licensee's role. There are, however, some general areas with which the licensee should be familiar. Responses to some of the following questions will vary from community to community or even within any given community:

1. What styles of architecture are common in your community and how are they best identified?
2. What are the approximate per square foot costs of homes of varying quality within your community?
3. Can you identify the different types and styles of windows with respect to location, function, materials and operating mechanisms?
4. What kinds of floor materials are available? What is the cost differential? What are the qualities of durability and comparative costs of installation and maintenance?
5. What are the materials most commonly used on the exterior surface of a house and what are the relative costs of installation, upkeep and market acceptance?
6. What are the different types of heating/cooling systems for a home and their relative costs of installation and operation?
7. What are current insulation standards for windows, roof, walls, and underfloor areas? What types of materials are commonly used?
8. What can be done to prevent termites, dry rot and other fungus and insect infestations?
9. What are the most desirable roof pitches and roofing materials? Can you distinguish a hip roof from a gable roof? What types of roofing materials are permitted in the community such as requirements for fire-retardant roofs?
10. What window coverings and window systems are available to prevent excess sun infiltration or water intrusion?
11. What are some common concerns about floor plans and specific rooms, i.e. separate dining or family rooms?
12. What kinds of materials are approved for use in the water and plumbing systems, i.e., pvc, copper, galvanized?
13. What kinds of materials are approved for use in electrical systems? What are some common devices that protect against overloading the system?
14. What is the condition of the soil on which the house is built? Is structural integrity jeopardized by filled ground? Slide conditions? Expansive soil? Drainage?
15. What restrictions, if any, run with the property?

