

Appraising Property with Entitlements: Value or Voodoo?

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Orange County Chapter

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Entitlements: No-Brainer to Brain Teaser

- On *newer, fully developed* properties- apparent and endemic property characteristic
- On *older developed properties*-implicates obsolescence and nonconforming use issues
- On *entitled but undeveloped* properties- implicates highest and best use issues
- On *unentitled properties*-let the voodoo begin! Issues of likelihood of obtaining, cost, risk, and value abound.



Highest and Best Use-the Analytical Starting Point



- Physically Possible
- Legally Permissible-(barriers to entry)
- Financially Feasible-(costs of obtaining, meeting conditions)
- Maximally Productive

Sales Comparison Approach

- For Permits Themselves-rare applications, but some have discernible markets, e.g., liquor licenses. (MMD permits??)
- For permitted properties-largely defines comparable sale set (hotels, gas stations, single family residential, warehouse, etc.)
- Evid. Code sec. 816



Sales Comparison Approach

- Trickier: Entitled but Undeveloped Property

Narrower Markets: (Developers usually develop, not sell) so finding comparables is often a challenge.

Defining the Entitlement's "Band of Value:" no improvements to use as a reference point for allocations

Entitlements as Changing the Unit of Value: instead of per acre or per square foot, market measures of per unit or per door.



One Solution: Replacement Cost

- Investigate (or estimate) the costs incurred to secure entitlements, and assign that as value
- Frequently seen in valuations during recession-entitlements had to be considered as value attribute, but no “value added” above investment
- Danger -“sum of the parts” valuation requires defensible appraisal judgment that second guesses the market participant itself (owner)
- Evid. Code sec. 820





Murkier Waters-Income Approach

- Legal Evidentiary Limitations:
 - Developer’s Residual Approach-in some contexts, cannot value non-existent improvements- *Contra Costa Water Dist. v. Bar-C Properties* (1992) 5 Cal. App. 4th 652 .
 - Nor can you value income streams from them-*S.D. Metro Transit Dev. Bd. v. Cushman* (1997) 53 Cal. App 4th 918
 - Nor Impute Better Income to Existing Improvements if Changed-*Redevelopment Agency of S.D. v. Mesdaq* (2007) 154 Cal. App. 4th 1111



Murkier Waters-Income Approach (ctd.)

- BUT:
 - You can value the inherent ability of a property to expand improvements them-*S.D. Metro Transit Dev. Bd. v. Cushman* (1997) 53 Cal. App 4th 918
 - And the likelihood of getting approvals for such improvements goes to weight, not admissibility (*Id.*)
 - **Appraisal foray into the metaphysical?** Assessing the *inherent potentiality* of added value, but only on what currently exists?
 - Evid. Code sec. 819

Mining Property-The Exception to the Rules

- For mining sites-a capitalized income stream from anticipated royalties is a permissible valuation for the owner's interest-even if permitting is needed. (*Ventura County Flood Control v. Campbell* (1999) 71 Cal. App. 4th 211). Considered like a measure of market rent
- Must value the material in place-not the business of mining (*City of Stockton v. Albert Brocchini Farms* (2001) 92 Cal.App.4th 193)



Emerging from the Murk

- Use Sales Comparison: if there is a market
- Use Cost Replacement: if there are entitlements, but they don't achieve highest and best use
- Use Income capitalization: with caution, and always with extraordinary presumptions or hypothetical conditions clearly identified





Surveying Land Use Entitlements

- Shift from broad methodology to practical considerations
- Specific types of land use permits properties can have
- Strengths and vulnerabilities
- Nuanced permit characteristics that may support appraisal judgments



Surveying Land Use Entitlements

- Examples of where characteristics of permitting/entitlements may affect appraisal conclusions:
 - Risk factors on income capitalization rates
 - Assessment of remaining useful life of improvements
 - Length of interim use periods
 - Damage analyses (impacts to permits themselves, or operational requirements they impose)

Zoning

- The “face” of a property
- Strengths:
 - Easily discernible
 - Strongest “surface” indicator of property type
 - Ability to show potential favorable change
(*People v. Arthofer* (1966) 245 Cal. App. 2d 454)



Zoning



- Weaknesses:
 - Rarely self executing (zoning as a matter of right)-frequently requires further permitting
 - No vested right to continuation-subject to amendment
 - Securing variances can be difficult and reserved for exceptional situations (Gov't Code sec. 65906)
 - No “use” variances
 - Special circumstances depriving property of privileges enjoyed by others
 - No special privileges

Legal Non-Conforming Use

- Permissive continuation of use/structure rendered non-conforming by change in zoning
- Can be positive impact on value (i.e., billboards); or negative (typically-destroyed structure cannot be replaced; change in use triggers need to come into conformity)
- Restrictions largely local (*but see* Gov't Code sec. 65852.25-multifamily housing to be allowed to rebuild)



Local Site Plan/Development Permits

- Strengths:
 - Site-specific
 - Flushes out discretionary conditions/exactions
 - Substantial expenditures or investments in reliance on valid building permit may result in vested rights-*Avco Community Developers v. South Coast Regional Commission* (1976) 17 Cal. 3d 785



Local Site Plan/Development Permits

- Weaknesses:
 - Often subject to unusual conditions (hours of operation, signage, etc.)
 - Subject to revocation or need for amendment with changes in use or surrounding circumstances, without clearly defined criteria (substantial discretion for local enforcement)





Conditional Use Permits

- Cal. Government Code sec. 65901
- Strengths:
 - Run with the land, and frequently recorded-transferable rather than personal to permit holder-
County of Imperial v. McDougal (1977) 19 Cal. 3d 505
 - Body of law on how/when CUP rights may vest-
Goat Hill Tavern v. City of Costa Mesa (1992) 6 Cal. App. 4th 1519



Conditional Use Permits

- Weaknesses:
 - Require local hearings-often site-specific politicization
 - Attachment to land tends to lead to more onerous conditions
 - Can be made revocable on defined terms/occurrences (but must have nexus to operations)

Tentative Parcel/Tract Maps

Subdivision Map Act (Gov't. code secs. 66410 et seq.)

- Strengths:
 - Primary discretionary step in clearing way for parcelization; market-recognized benchmark for entitled property
 - Defines in quantifiable terms dedications, infrastructure improvements, fees



Tentative Parcel/Tract Maps

- Weaknesses:
 - By itself, doesn't confer right to sell lots
 - Two year limitation unless extended (Gov't. Code sec. 66452.6-*but see*-automatic 24 additional months per sec. 66452.24)



Final Tract Map/Parcel Map

- Cal. Gov't Code sec. 66456 et seq.
- Strengths:
 - Confers the legal right to sell, mortgage, or hypothecate individual lots
 - Generally, ministerial to obtain upon meeting tentative map conditions
- Weakness:
 - Does not by itself insulate against changes in zoning or land use



Vesting Tentative Map

- Cal. Gov't Code secs. 66498.1 et seq.
- Strengths:
 - Insulates the subdivision from future changes in land use standards
 - Confers the right “to proceed with development in substantial compliance with ordinances, policies, and standards” in effect when map application deemed complete.



Vesting Tentative Map

- Weaknesses:
 - Purely discretionary
 - Vesting nature requires more advance work than traditional tentative map- (Gov't Code sec. 66498.8)
 - Time limits on vesting are limited by local ordinance (1-2 years after filing of final map, per Gov't. Code sec. 66498.5(b).)





Development Agreement

- The “Gold Standard” of Entitlements
- Cal. Gov’t. Code secs. 65864 et seq.
- Strengths:
 - Protects against changes in zoning and fees
 - Negotiable duration (5-20 years typical)
 - Contract with agency-so contract remedies available for enforcement



Development Agreement

- Weaknesses:
 - Difficult to Obtain
 - Ordinance required to adopt-implicates public hearings, subject to referendum

Conclusions

- Entitlement valuation is routine on established properties, but can be more complicated on undeveloped ones
- Valuing entitlements can entail both valuing the entitlement itself, or its impact on the property
- The nature of entitlement, and nuances of its characteristics, can be utilized as support for appraisal value and damage judgments

Questions?