Estimating Hotel Land Values Using Comparable Ground Leases

The following article by Stephen Rushmore, MAI, is reprinted with permission from "Rushmore on Hotel Valuations" (Winter 1980).

As a hotel appraiser, I am sometimes called upon to estimate the value of a total property and also to break out a separate land value. Following normal appraisal practices, one would first investigate the market for recent land transfers of vacant parcels having similar characteristics such as size, street frontage, location and zoning. Any differences between the comparable and the subject would then be adjusted through the use of an adjustment grid. In reality, this process is often difficult to accomplish due to the lack of sufficiently comparable vacant land sales data and the inability to estimate necessary adjustments properly. An alternate approach, based on the premise that the value of land is tied directly to its income generating capability at the highest and best use, might be termed the "comparable ground lease method."

Each year a number of hotel transactions are structured using ground leases. Typical rental terms vary from simple flat payments with escalation adjustments to formulas based entirely on gross revenues. From a land valuation viewpoint, the net rental using a percentage of gross revenue most closely fits the appraiser's objective of quantifying a pure income attributed to the land.

The following example shows the procedure.

Number of rooms	200
Projected room revenue	\$1,915,000
Projected food revenue	\$1,150,000
Projected beverage revenue	\$ 575,000

Eight ground leases for motels similar to the subject were found. Their rental formulas are shown in the chart below. The estimated ground rental for the subject is calculated using the comparable formulas and the subject's projected revenues.

If all the comparables were equally similar to the subject, the average ground rent of \$102,437 would be a supportable estimate of the income attributed to land. The value of the land would then be calculated by capitalizing the subject's estimated ground rent by an appropriate capitalization rate:

$$\frac{\$102,437}{.11} = \$931,245$$

Land value (say) \$930,000

The example shows a land value of \$4,650 per room which is within the current range of standard quality motels (see "Rushmore on Hotel Valuations," Fall 1979). For recently constructed lodging facilities, a quick land value cross-check can be made by seeing if the land value is within the normal limits of 10% to 20% of the total project cost.

Data pertaining to 17 hotel ground leases involving airport located lodging facilities have been compiled by Helmsley-Spear Hospitality Services, Inc. A synopsis of rental terms for these properties can be obtained free of charge from Stephen Rushmore, MAI, Hospitality Valuation Services, 22 Shepherd Lane, Roslyn Heights, NY 11577.

Comparable Number	Fixed Rental (per Room)	Percentage of Gross: Room Revenue	Percentage of Gross: Food Revenue	Percentage of Gross: Beverage Revenue	Subject's Estimated Ground Rental
1	None	3%	1%	1%	\$ 74,700
2	\$257	3	—	—	108,850
3	None	7	—	—	134,000
4	\$ 72	4	—	—	114,000
5	\$149	2	1%	1%	85,350
6	None	5	—	3%	113,000
7	None	4	1%	1%	93,850
8	None	5	—	—	95,750
				Average	\$102,437