



Buying Rural Land? Learn These Loan Facts First

By Lynne Hayes, Growing America

Whether you're a new landowner buying your first 40 acres or a 3rd generation owner looking to expand what your grandparents started, seeking a rural land loan can be downright confusing.

Finding out interest rates and terms for rural land loans are different from home loans often surprises buyers, but the reason is pretty simple: it comes down to risk.

Lenders consider land loans to be higher risk compared to home loans, and rightly so. Homes located in neighborhoods are usually easier to value due to readily available comparable sales. These sales help determine how the home will hold its value. A piece of rural land is more difficult to match with a comparable sale and is subject to many unknowns when it comes to future performance.

A landowner experiencing financial stress, for example, may have to make difficult decisions about which debts to continue paying and which loans to let go delinquent. Keeping a roof over a family's head would likely take precedent over saving a piece of land, especially if the land does not produce income. Of course, the delinquency can leave the lender high and dry. Bottom line? Land loans are riskier and this makes them a little pricier for the borrower.

Yet, while the interest rate does matter, it's only part of the story when it comes to selecting the right land loan. Jesse Dumas, an experienced rural lender, helps shed light on important things to know before you borrow.

Different Institutions, Different Rates

"Your choice of lending institution can make a big difference in your total interest cost, and often it has little to do with the initial interest rate," says Dumas.

"Commercial banks lend, in part, based upon deposits which typically have short maturity cycles (for example, a certificate of deposit). As a result, they aren't likely to fix your interest rate for more than 3-7 years," he adds. "Assuming no repayment issues, your loan will usually be renewed when it matures. However, it will be renewed at prevailing market interest rates, which could be much higher than when the loan was first approved."

In contrast, Dumas points out that Farm Credit doesn't collect deposits and loan them back out. Instead, loans are funded from the sale of their own debt instruments—called bonds—in the nation's money markets. If you want a 20-year fixed rate on your land loan, Farm Credit raises those funds by borrowing 20-year money from investors and lends that to you. The longer fixed rate is slightly higher, but for you as the borrower all risk of a significantly higher payment and increased interest cost when a shorter-term rate must be renewed is eliminated.

"By offering both short and long-term rate options," says Dumas, "the customer gets to decide if they prefer to pay a little more today to avoid an unknown rate and payment increase in the future. Our customers like having that kind of choice."

Even though we deal with rural land daily, we know for most people buying land is not something they do often.

More to Consider

It's important to ask the lender how long they're willing to set up the term of the loan, with 15 to 20 years being typical. A longer loan term can help make your payment more affordable, which is important. Yet, a longer loan term likely means at least a small increase to your interest rate.

If your dream, now or in the future, is to live on your land, be aware of limits on how much acreage can be financed with your home. "People are often surprised when they're told the home they want to purchase or build includes too much land," Dumas says. "Farm Credit's rural lending focus frees customers from any acreage limitation."

Down Payments Differ, Too

Along with different interest rates and loan terms, it's also important to understand the down payment requirements for land loans will differ from home loans.

"For a land loan, it's not unusual to be required to put down 30-40% of the purchase price with the other 60-70% percent of the cost being financed," explains Dumas. "Farm Credit typically asks a customer to put down 15-25% and finances between 75-85% of the purchase price."

Farm Credit can also finance some transactions at 100 percent if the situation is right, Dumas adds, "If a buyer already owns land and has enough equity in it and no loans against it, the land can make excellent additional collateral. For some people, this option works well."

Other Expenses to Keep in Mind

It's important to know land loans can have other expenses—not hidden mind you, but not always considered until the final tally. The terms of the sale often leave room for negotiating whether the buyer or seller pays for some of these expenses.



Land loans generally include an origination fee (essentially a fee for activating a loan account), along with title insurance (which helps you and the lender ensure you have clear title to the property), plus a fee for an appraisal and possibly a land survey. Some states add fees for documentary stamp and intangible real estate taxes on new mortgages. It's worth noting, Dumas points out, when a mortgage is filed in the state of Florida, Farm Credit customers are exempt from paying documentary stamp and intangible real estate taxes.

Certain pieces of land also include features requiring the purchase of insurance. Suppose the land you want has a cabin or barn on it; such an improvement adds to the appraised value of the property. Additionally, the buyer is usually required to carry hazard insurance to protect themselves and the lender from risk of loss or damage. What's more, if the improvement is in a designated flood zone, lenders must require flood insurance.

Each Situation is Unique

Along with different loan factors, there are issues from A (access) to Z (zoning) to consider about the land itself.

When buying land or a home with acreage, a number of issues need to be considered, or considered from a different perspective, than those associated with purchasing a residence.

“It’s important,” Dumas says, “for you and your lender to discuss your plans for the land along with your finances to ensure they understand your unique situation.”

“Even though we deal with rural land daily,” he adds, “we know for most people buying land is not something they do often. Beyond selecting the best loan terms, talking with a knowledgeable rural lender may help you avoid common, yet at times costly, mistakes.”

It Pays to Ask the Right Questions

Yes, it really does pay to ask the right questions when shopping for the best land loan.

“People call and are tempted to just ask our rate and then try to make comparisons,” shares Dumas, “but the rate alone can’t tell you what you really need to know.”

“When you ask about the rate, remember to also ask how long the rate can be fixed,” he advises. “If you compare a 5-year fixed rate to a 15-year fixed rate, it’s not an apples-to-apples comparison.” Dumas adds you’ll also want to understand the loan term, down payment requirement and other expenses.

When it comes to loan cost, Dumas makes this interesting point: “Farm Credit customers become members of the cooperative when they borrow. Each year, earnings above what is needed for capital and to operate are returned back to our members, lowering their total loan cost. Essentially, instead of paying dividends to outside stockholders, a part of the interest paid is eligible to be returned to them.”

Final Advice? Be Prepared

Dumas’ final piece of advice to those buying land is, “the best kind of buyer is a well-prepared buyer.” He recommends getting pre-qualified for your loan before starting your land search. By doing so, you have a chance to ask questions and gain confidence about your shopping budget and the land buying and financing process. It also shows the real estate agent you’re a serious buyer and can help ensure a smooth transfer of ownership when the time comes.

No matter the purpose: future home site, timberland, farming, hunting, fishing or rural lifestyle, let Farm Credit help with a loan structured just for you. Whether buying, refinancing, or making land improvements, contact a rural lending specialist at GoRural.net or 855-GoRural. Let Farm Credit take the risk of rising interest rates off your shoulders with a long-term fixed rate.