

Real Estate Investor Insights

Lead Story: Creating and Monetizing Value in owned Real Estate

When you own the business and the real estate:

Many business owners also own the real estate that houses the business. Clearly there are many benefits to owning real estate vs. leasing, not the least of which is the ability to monetize it. It can also create a cash flowing generational annuity. While there can be many benefits it is critical that whatever strategy is employed it does not adversely affect the performance, and value, of the operating company.

Finance the real estate: Given the low interest rate environment, securing a low leverage loan on your property may make sense depending upon the exit strategy of the business. If you are planning to keep the business in residence then long-term debt is a great option. However, if you are considering an exit in the near term, while debt is still an option, all the terms of the credit facility, including rate, term, defeasance (prepayment) and loan assumption need to be carefully considered.

Note: If you sell the business, and that entity also acquires the real estate, your ability to pay off the debt cost-effectively (or if the loan is attractive—have the debt assumed) is very important.

Sale/Leaseback: Today there is an abundance of capital seeking to buy properties with long-term, credit leases in place so if you can structure a market lease in your property investors will pay a premium. Credit and term usually drive value unless your property has redevelopment potential.

When considering this, you first must have clear understanding of the tax consequences. Equally important is to *structure a lease that is marketable to investors but that also protects the business. That includes building in flexibility so the lease does not encumber the eventual sale of the business, while also incorporating some protective covenants, like buy-back provisions, in the event the new owner elects to sell the property in the future.*



With proper planning owned real estate that is held by the business can be a great source of revenue and in some cases be more valuable than the operating company itself

Selling your business and retaining ownership of the real estate.

Sounds great right?! You sold your company, secured a 5 year lease with options, are still involved given you have an earnout, and the Private Equity company assured you they would not move out. *Fast forward 2 years*—you are no longer involved with the company, they are considering not renewing and may be relocating sooner, and you now want to sell or refinance the building. Unfortunately **the market (including lenders) may deeply discount the property** given that the future of the tenant is uncertain, and you cannot predict future cash flow.

An interesting dynamic occurs as the primary purpose of the real estate shifts from supporting the business to a real estate investment

Congratulations—you are now a real estate developer! You now need to begin planning for the process of re-leasing the property, which includes setting aside capital for building improvements, brokerage commissions, and possibly additional reserves for the bank. In addition, you cannot predict how long the space may be vacant, what the new tenant will pay, and what their credit standing is. *Whether you are seeking to sell the real estate post-sale or retain it for the cash flow, the key is to structure a lease which protects your future financial interests and do so as an integral consideration of your business sale.* With the right lease in place, the real estate could be worth more than your business. Without it, you could be a greater financial risk than you realize

Plan, Plan, Plan: Even if you do not have immediate plans to sell, it is critical you work with your financial and real estate advisory to determine the potential value of business and real estate well in advance of any sale. In that way you are then better prepared to make informed decisions which will increase value for both business and real estate, and create more transitional wealth for your family.

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