

Business Succession in Real Estate

Succession strategies and maximising value

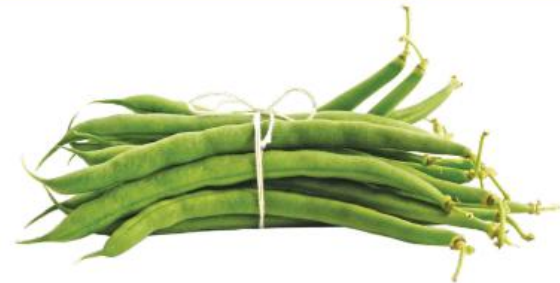
Friday 15th July 2011

Paul Brooks



John Knight

UHY Haines Norton
Chartered Accountants



not your average *Bean* counters

Succession 

= Value

Succession

= Value

**that can be passed on to a successor
or that someone is willing to buy.**

Overview

Types of succession.

Stages of succession.

What is value?

Drivers of Value.

Improving Value.

Maximising after-tax dollars.

Feel free to
ask questions
as we go.

Types of Succession

Complete Business sale

Entity sale (partial or full)

Family generational transition

Manager / Key Person Buyout

Gift versus sale

Part Owner Transition

Partnership Breakup

Structured Liquidation/Sell-down

Key Person Death or Disablement

Stages of Succession

- 1. Planning for succession** — 3-5 years out
 - 2. Preparing for succession** — 2-5 years out
(value enhancement & successor identification)
 - 3. Marketing**
 - 4. Negotiating & Documenting**
 - 5. Settlement** — 90 days for retention plus vendor finance
- Allow 6-9 months

Stage 1. Planning

Position assessment

Financial analysis (trends)

Undertake the diagnostic

www.uhyhnbrisbane.com.au/succession_diagnostic

What is the most likely strategy?

What unlikely events could occur?

When is it likely to become an issue?

Structure and tax review

Review non-business investment strategy

Indicative valuation

**So what is value and
(more importantly)
what is the value of
your business and the
assets connected to
your business?**

Value

Cash

Fair Market Value

Fair Market Value

- **the price that would be negotiated between**
 - knowledgeable & willing but not anxious buyer &
 - knowledgeable & willing but not anxious seller
- **in an open and unrestricted market**
- **acting at arms length**
- **within a reasonable time frame**

Value

Cash

Fair Market Value

Value versus Price

Business versus Entity

Valuation Methodologies

Valuation Methodologies

**Outside of Real Estate =
Capitalisation of FME**

**Real Estate =
Rule of thumb for rentals
+ Something for Sales
(usually nominal)**

How much would it cost to setup from scratch?

Rule of Thumb Check

Gross Commission Income pa	\$600,000
Rule of thumb multiple	2.75 times
Value	\$1,650,000

Net Profit PM (Before finance & owners remuneration)	\$330,000*
Multiple of Profit	5 times

Net Profit PM (After bank interest & allocation of owner remuneration but before tax)	\$210,000
---	-----------

Multiple of Profit	7.9 times
--------------------	-----------

* after allocation of 50% of overheads

** after allocation of 50% of overheads and before principle debt repayments

No doubt the greatest value in a real estate business is in the rentroll.

So what are the key drivers of value in a rentroll and how do you maximise this value

Paul Brooks

Slides deleted as requested



Stage 2. Preparing

Make necessary changes to costs

Secure staff (as much as you can)

Reports to provide necessary information

Reduce reliance on key people

Reduce unnecessary expenditure

Maximise staff productivity

Isolate or remove directors benefits

Transfer non-business assets/liabilities

Could you sell the entity?

Systems and Procedures – document.

Improving Value

Increase Profitability

Improve Opportunities

Improve Efficiency

Reduce Waste

7 Deadly Wastes

- 1. Overproduction**
- 2. Waiting**
- 3. Transporting**
- 4. Inappropriate Processing**
- 5. Unnecessary Inventory**
- 6. Unnecessary Motions**
- 7. Defects**



Improving Value

Increase Profitability

Improve Opportunities

Improve Efficiency

Reduce Waste

Reduce Risks

Improve Corporate Governance

Corporate Governance

**Correlation between good governance
& a valuable business.**

**Separation of private wishes from the
corporate good.**

Board Meetings.

Advisory Board.

Stage 3. Marketing

Confidentiality

Information presentation

What do the banks want?

What do the valuers want?

What do the buyers want to see?

Specialisation

Realistic expectations and timeframe

Stage 4. Negotiating & Document

Involve your advisers (they may want to change the structure of the deal)

Document agreement (everyone needs to be on the same page)

Try and remove the emotional connection

Steps to complete succession

Profit share v equity

Transparency

**Assuming you have
maximised the value of
your business/entity.**

**How do we now
minimise tax and
maximise cash?**

Tax Considerations

Income Tax

Retained profits (franking credits)

Capital gains tax (CGT)

Small Business CGT Concessions

Stamp Duty

Super Strategies

Sale of Business

Contract Date

Sale of business or sale of shares?

**Restructuring for Sale
(just before sale?)**

Contract terms – apportionments

Sale to Family – no cash paid!

Sale of Business

**Vendor finance or delayed payments
(Earnouts or Clawbacks)**

**Accessing sale proceeds
(when does tax stop?)**

**Company v Unit Trust v
Discretionary Trust v Individual**

CGT Discounts/Concessions!

General 50% CGT discount (individuals)

50% Active Asset discount

Small business rollover (2 years)

Retirement exemption – Super

15 year exemption

Small Business
CGT Concessions

CGT Concessions!

1. Are you small?

- **\$2m turnover**
- **\$6m net value of assets**

2. Active Assets?

- **Are the assets active/business?**
- **80% test for shares**
- **Active for 7.5 years or 1/2 ownership**

3. Are you Significant?

- **20% test or 90% test**

Note: This is an over-simplistic summary of the key tests – this is a complex area of tax legislation – you must seek professional advice on your specific situation.

CGT Concessions!

If under 55 years of age – balance of gain may need to go into super to make tax free.

If over 55 years of age – cash can usually be taken personally.

Use concessions to bulk up super.

Consider restructuring now – why?

- **before value increases further**
- **minimise stamp duty (if applicable)**
- **get proceeds into super**
- **fix structure**

Minimising Tax

Some of the best tax planning strategies are tax deferment

Tax avoidance v tax planning

Structure has a big impact – don't leave until too late – 0% v 30% v 46.5%

Personal low rate thresholds

Stamp duty savings – take a hit

GST considerations – going concern?

Super strategies (self managed super)

Tax savings – cash in hand?

	Revenue \$	Capital \$	Concession \$
Net sale proceeds	1,000,000	1,000,000	1,000,000
less:			
50% General CGT Discount > 12 months	-	500,000	500,000
	1,000,000	500,000	500,000
less:			
50% Active Asset discount	-	-	250,000
	1,000,000	500,000	250,000
less			
Retirement exemption	-	-	250,000
	1,000,000	500,000	-
"Taxable Income"	1,000,000	500,000	-
Tax Paid @ 46.5%	465,000	232,500	-
Cash in hand	535,000	767,500	1,000,000

Stage 5. Settlement

Retention period

Funding issues

Do you need cash for some other reason – to put into super?

Have you agreed to vendor finance terms?

**What else should you
be thinking about?**

Unforeseen Succession

Death or disablement

Personal events

Keyperson insurance

Buy-Sell Agreement

Life/TPD Insurance

Other assets and income streams

Wills & Estate Planning

Barriers

succession

Are you ~~investor~~ ready?

Would you buy your
business?

What would you look for?

Who is your successor?

What is your next step?

To help, try the succession planning diagnostic at [www.uhyhnbrisbane.com.au/succession diagnostic](http://www.uhyhnbrisbane.com.au/succession_diagnostic)

Questions?



Thank You

Slides will be available at
www.uhyhnbrisbane.com.au.

John Knight
UHY HAINES NORTON

j.knight@uhyhn.com.au
www.uhyhnbrisbane.com.au
Direct phone 07 3210 5513
Mobile 0438 68 7751
Twitter: [jak_knight](https://twitter.com/jak_knight)



Paul Brooks
REAL ESTATE DYNAMICS

paulbrooks@realestatedynamics.com.au
www.realestatedynamics.com.au
Phone 07 3720 9344
Mobile 0419 731 390

