SALES ASSOCIATE COURSE

CHAPTER 17

Real Estate Investments and Business Opportunity Brokerage

Investment Analysis

- **Most important consideration:**
  - **Economic soundness**
- Land use controls
  - Zoning
  - Deed restrictions
  - Permitting requirements
- Economic force
  - Population growth
  - Foreign capital
  - Impact of taxation

Investment Analysis

- **Advantages**
  - Income
  - **Equity build up**
  - Appreciation in value
  - Tax benefits
  - **Positive leverage**
  - Prestige

Investment Analysis

- **Disadvantages**
  - **Illiquidity**
  - Immobility
  - Expense/overhead
  - Additional expertise from
    - Real estate brokers
    - Tax accountants
    - Attorney's etc.

Types of Investment Properties

- Agricultural
- Business Opportunities
- Commercial
- Industrial
- Office
- Residential
    - Condominiums
    - Villas
    - Single family homes
    - Apartment complexes

Real Estate Investment Trust (REIT)

- Individuals pooling their resources for investment
- Professionally managed portfolio
  - Real property
    - Office buildings, apartment complexes, retail centers
  - Mortgages secured by real property
- Similar to mutual fund

Static vs. Dynamic Risks

- **Dynamic risk**
  - Associated with general market conditions
  - Cannot be shifted to an insurer
- **Static risk**
  - Can be transferred to an insurer
  - E.g. fire, theft or vandalism

Dynamic Risks

- Dynamic risk comes in many forms
  - Business
  - Financial
  - Inflationary
  - Interest rate
  - Liquidity
  - Market

Leverage

- Use of borrowed funds, or OPM - other people's money; (AKA "trading on the equity")
  - **Positive leverage**
    - Rate of return greater than interest rate (increased return by borrowing)
  - **Negative leverage**
    - Rate of return less than interest rate

Reconstructed Operating Statement

Potential **G**ross **I**ncome		**PGI**	(or GI)
Vacancy and **C**ollection loss allowance	-	**V&C**	(% or $)
Other **I**ncome	+	**OI**	
Effective **G**ross **I**ncome		**EGI**	
Operating **E**xpenses	-	**OE**	
Net **O**perating		**NOI**	
Annual **D**ebt **S**ervice	-	**ADS**	
Before **T**ax **C**ash **F**low		**BTCF**	
Income **T**axes	-	**TX**	
After **T**ax **C**ash **F**low		**ATCF**	

Operating Expenses

Fixed **E**xpenses

- Property Taxes
- Hazard Insurance

Variable **E**xpenses

- Maintenance
- Utilities
- Management fees

Reserve for Replacements

- Noncash expense
- Use in the future to replace worn out components

FE

VE

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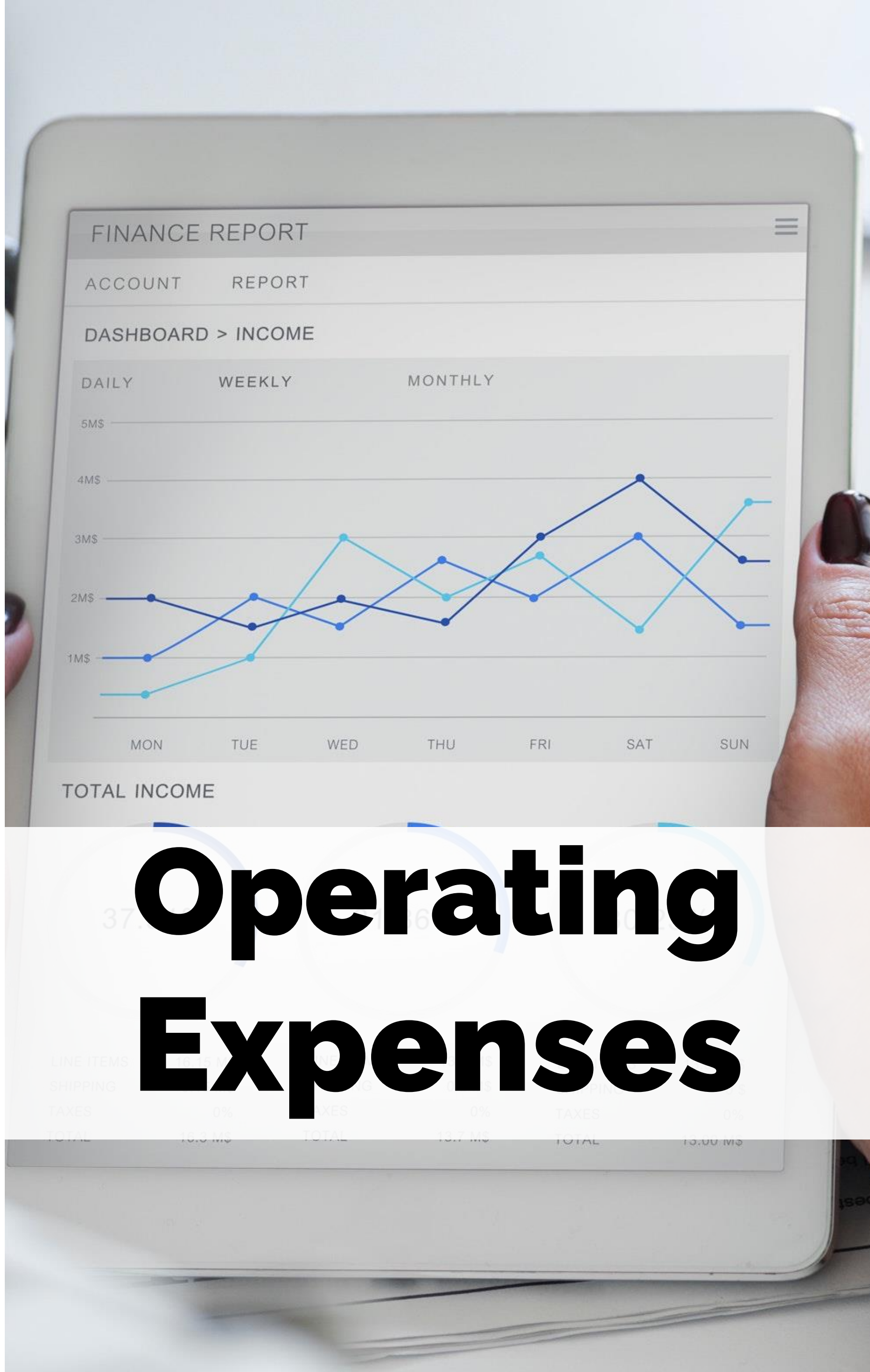
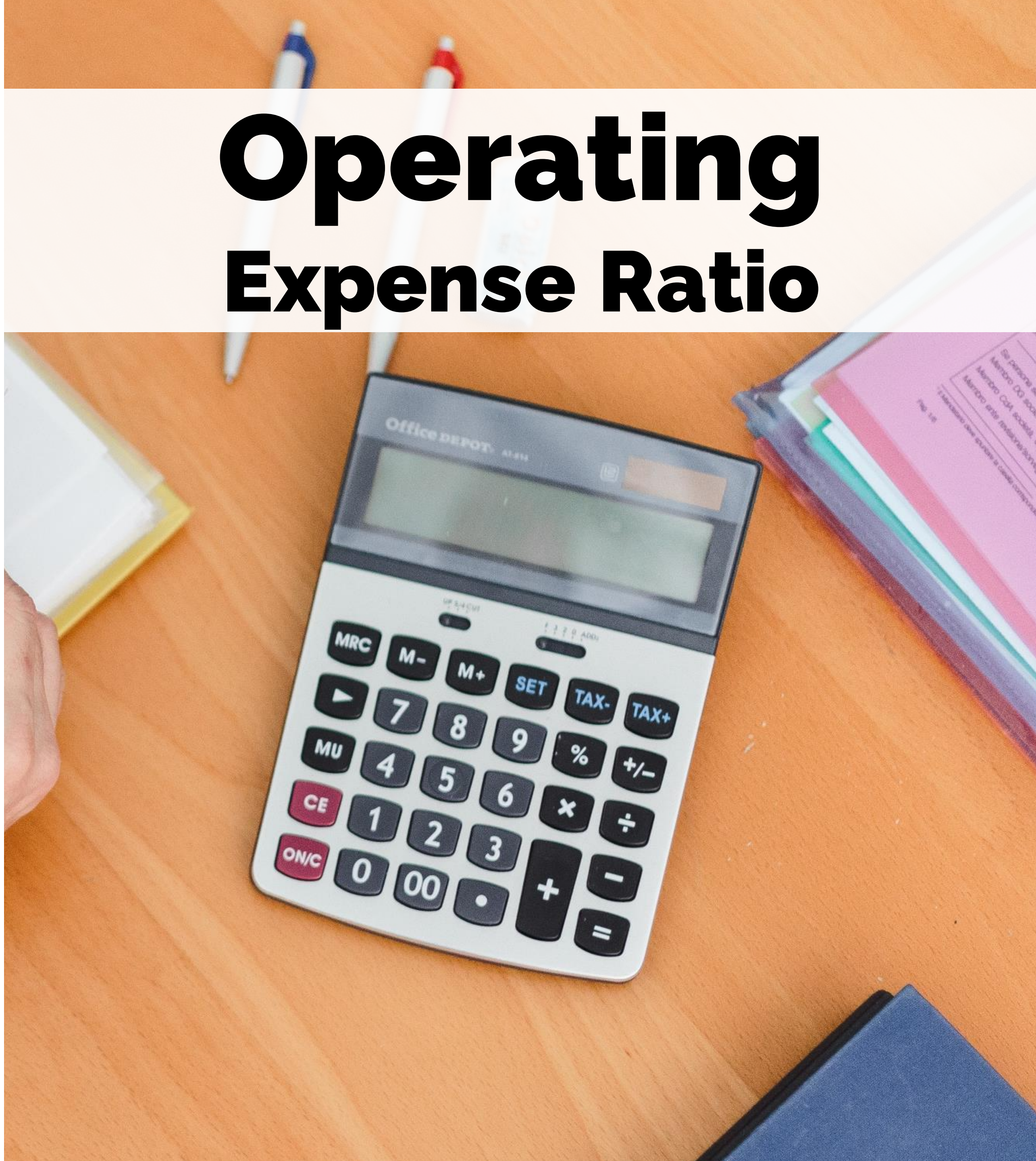
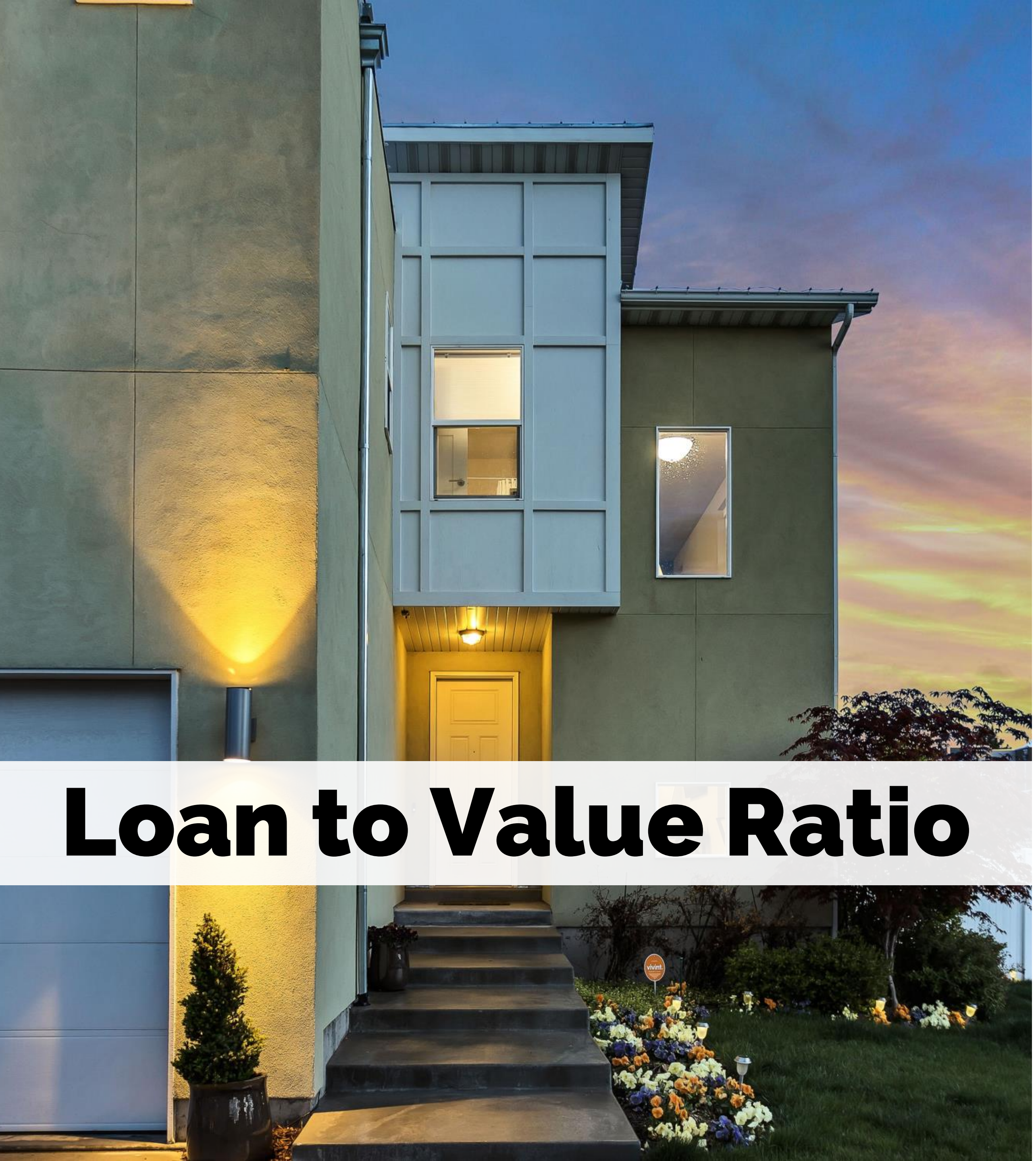


Operating Expense Ratio

$$\frac{\text{Operating Expenses}}{\text{Effective Gross Income}}$$

Provides for comparison with similar properties





Loan to Value Ratio

$$\frac{\text{Loan}}{\text{Value}}$$

Shows the % of value the lender agrees to lend

Calculating Profit on Investment

$$\frac{\textbf{Made}}{\textbf{Paid}} = \textbf{Profit or loss \%}$$

An investor paid $300,000 for a parcel of land and sold it for $200,000. What was the percentage of profit or loss?

$$\frac{\textbf{(\$100,000)}\ \text{loss}}{\textbf{\$300,000}} = \textbf{33\% loss}$$

Calculating Profit on Investment

Made
Paid **= Profit or loss %**

An investor paid $300,000 for a parcel of land and sold it for $400,000. What was the percentage of profit or loss?

$100,000
profit
$300,000

= 33% profit

Tax Shelter

- An investment that shields income from taxation
- Positive Cash Flow as property appreciates is ideal
- Tax shelter obtained by deducting interest and depreciation - especially depreciation - from net operating income

Business Brokerage

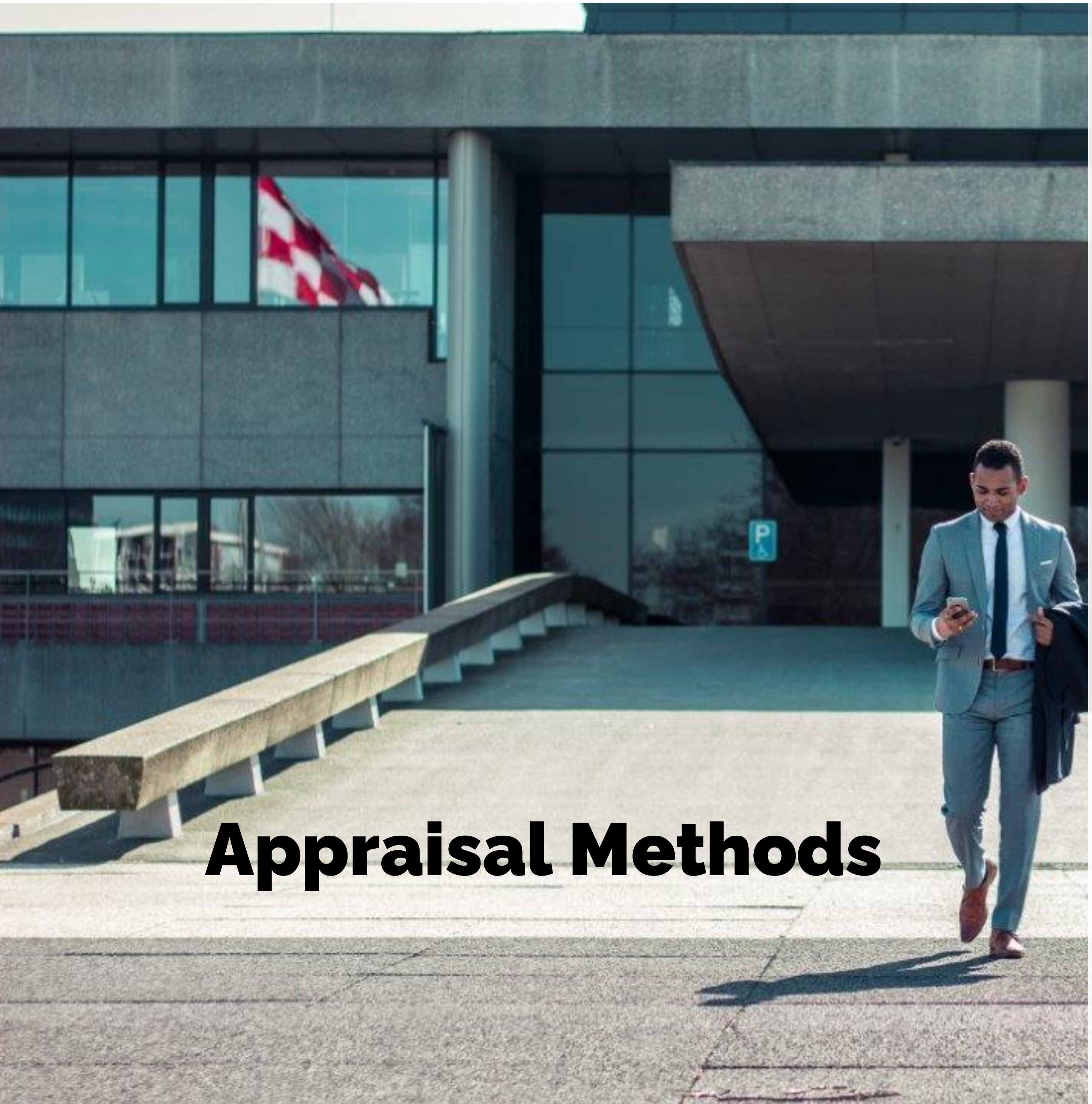
- Analyze financial statements
  - Reconstructed operating statements
  - **Balance sheets**
  - **Income statements**
- **Business brokers**
  - Sale, purchase or lease of a business
  - **Must hold real estate license**
- **Business Enterprises**
  - Transactions over $200,000
- **Business Opportunities**
  - Transactions under $200,000

Business Brokerage

- Sales frequently involve
  - Shares of stock
  - Limited partnership interests
  - Securities
- Be careful
  - May violate securities laws
  - Requires separate license

- **Comparable Sales Approach**
- **Cost-Depreciation Approach**
- **Income Approach**
- **Liquidation Value Approach**
  - Value a failing business
  - Sell assets, pay liabilities
  - Minimum value of a profitable business

Appraisal Methods



Appraisal Methods

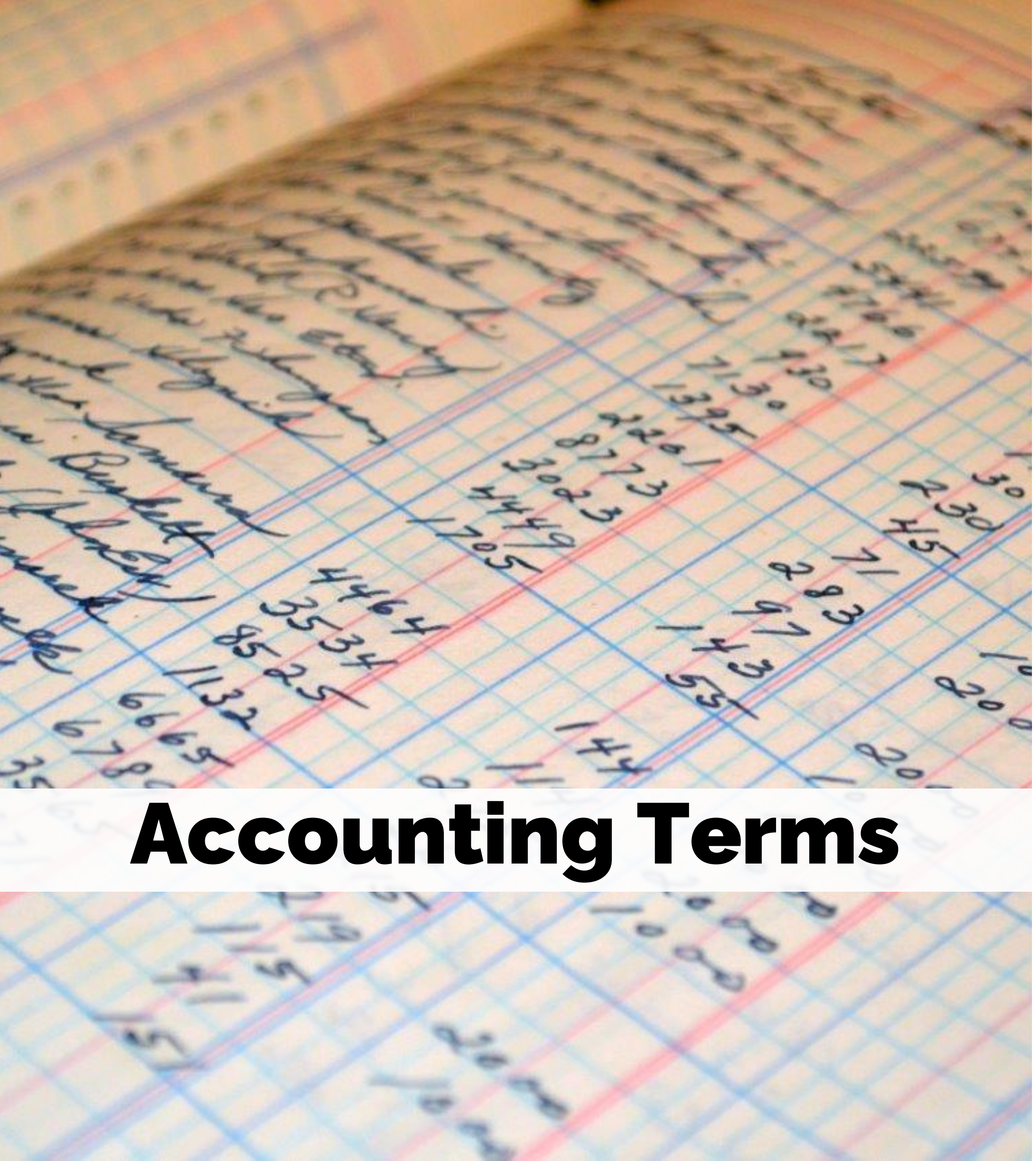
- **Going Concern Value**
  - Value of an established, profitable business in excess of the value of the physical assets
  - Includes:
    - Real estate
    - Personal property
    - Licenses
    - Franchises,
    - Non-compete contracts

Reason for a Business Appraisal

- Sale / Purchase, etc.
- Obtain loan / insurance
- Condemnation
- Buy-sell agreements
- Property settlements
- Estate settlement
- Assign values for stock option plans

Uniform Commercial Code

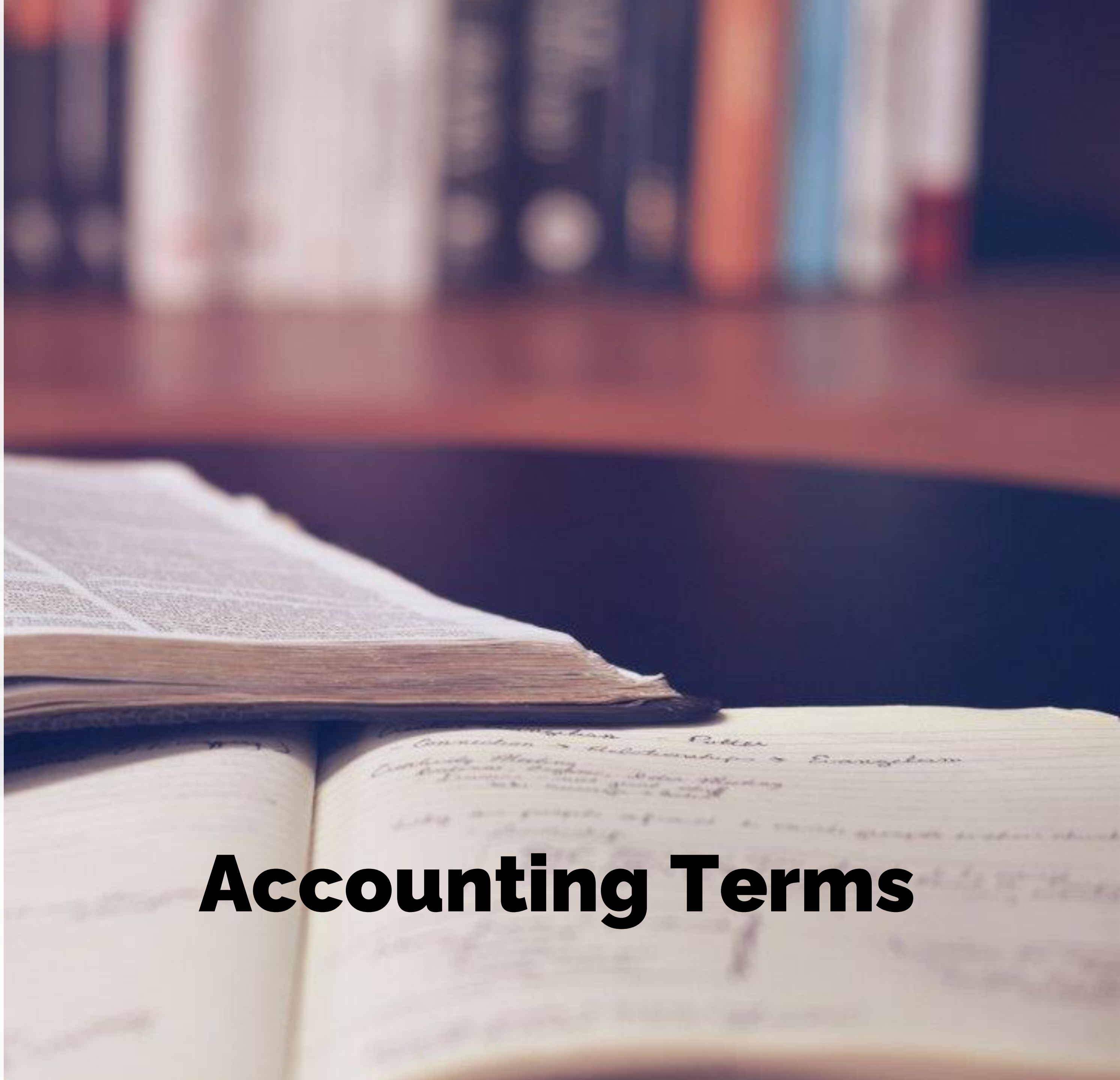
- Standardized rules that regulate commercial transactions throughout the U.S. pertaining to personal property
- Two documents:
  - **Bill of Sale** – used to identify property being conveyed
  - **Security Agreement** – financing of the business



Accounting Terms

- **Assets**
  - Tangible & intangible resources
- **Liabilities**
  - Short-term & long-term obligations
- **Owners' equity**
  - Assets minus liabilities
- **Capital**
  - Owner's equity or net worth

Accounting Terms



- **Tangible assets**
  - Buildings, furniture, equipment, etc.
- **Intangible assets**
  - Stock shares
  - Trademarks
  - Copyrights
  - Research & development expenses
  - Franchises
  - Goodwill

Steps in the Sale of a Business

- Acquire the listing
- List the assets
- Valuation
- Deduct liabilities
- Valuation of stock
- Legal compliance
- Close the transaction


Coffee Break
15 Minutes