mrmfinance

Management Rights & Motel Finance Pty Ltd

Guide to management rights

The smart choice

Hospitality, and the management rights industry in particular, is as familiar to me as the founding principles of accounting. My parents, siblings, friends and even my immediate family have all owned and managed management rights, and I have personally been involved in advising and arranging finance for many hundreds of new and existing operators – some as many as six and seven times over. I guess you could say that management rights is in my blood.

Mark Ryall

Established in 2005, Management Rights & Motel Finance PL (MRM Finance) has proved themselves as market leaders in finance options for the accommodation industry, successfully assisting thousands of clients with finance for management rights and motel transactions.

Clients of MRM Finance – many of whom have been with the company for more than 20 years - receive specialised advice and solutions to tailor their finance options, but the benefits of working with Mark Ryall and the team go beyond just assistance with the finance. MRM Finance are able to assist with best practices, licensing, bank accounts, merchant facilities, business plans, insurance, and many other templates.

MRM Finance has established strong working relationships with management rights industry professionals that ensures clients receive streamlined information and reporting due to the cooperation and communication amongst solicitors, accountants, financiers and brokers.

Having personally purchased ten buildings over the last 19 years covering permanent, holiday, student, corporate and mixed-use properties, MRM Finance also has a strong understanding of the specific acts governing the management rights industry.

Despite the 'personal approach' where clients are treated like family, MRM Finance has the resources and capabilities of a large firm as can be attested to by those who have been clients for more than 20 years across a multitude of transactions.

Industry

> *I treat every one of my clients like my parents. I get involved in their business, sharing best practice learnt from many years in the industry and my own family, and enjoy helping new operators overcome the vertical learning curve. It's tremendously rewarding watching a client start their journey in management rights and helping them through to a successful retirement.*
>
> ***Mark Ryall***

Why management rights?

Whether it is a combination of investment return, a combined home and business environment or the purported lifestyle aspect, if managed well, management rights has proven to be a very lucrative business proposition.

Even today, management rights remains the lowest risk going-concern business model in Australia, and it doesn't suffer from the normal issues that most businesses have – they don't have bad debts, there are limited debtors and creditors – and if there are the resident manager is in control of them, the cash flow cycle tends to be 30 days max and even then the resident manager gets paid first.

Ultimately, you have security of terms and the rights to buy into the management of a multi-billion dollar asset for a fraction of that.

specialist

> *I have known Mark for 12 years now and we have invested in partnerships with him seven times. Mark is very knowledge, professional, reliable, honest and very helpful. He is great at relationships and customer service and sets up partnerships with care so that the people involved can work well together. He always has time for you and any queries you may have and deals with difficult situations very well. Mark goes the extra mile when necessary and always keeps in touch with his clients, even after the completion of the purchase to ensure everyone is going along okay.*
>
> *I cannot recommend him highly enough and my husband and I would not work with anyone else.*
>
> ***Sue Williams***

What are management rights?

Evolved in Queensland during the early 1960s to address the accommodation need for a burgeoning tourism industry, management rights is a business platform that enables the appointed resident owner of a lot contained within a community living complex, to fulfil the role of caretaker/facility manager and to operate a letting business (of units within the complex) on behalf of non-resident owners.

The said appointed person, who owns the management rights, is usually referred to as the resident or onsite manager.

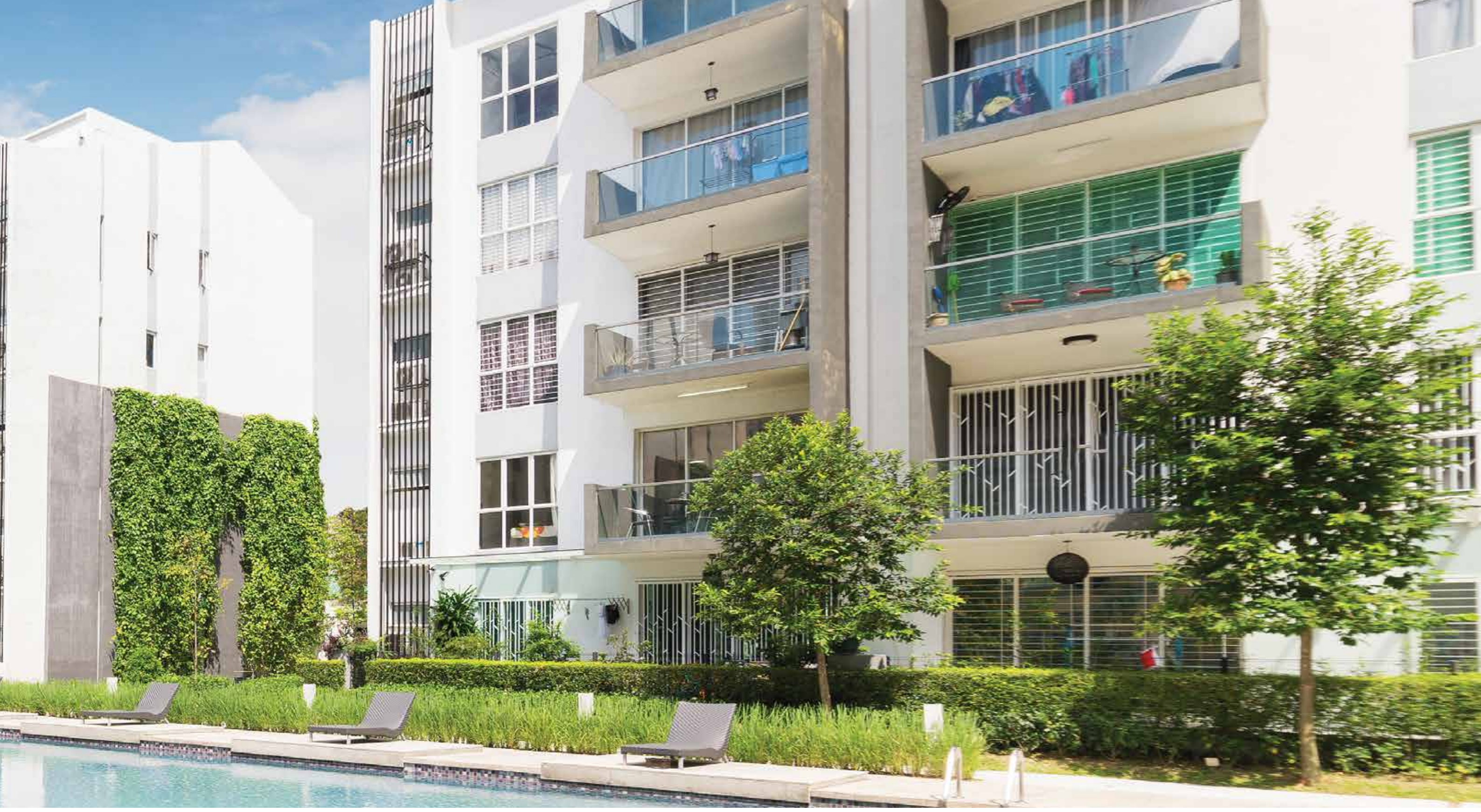
Typically, having management rights to a property development means you:

- Live on the property
- Take care of common property on behalf of the body corporate (as per an agreed schedule of duties)
- Let units in the complex on a rental basis. Please note that to be able to operate as a letting agent, you will acquire a licence. (For more information, see the section on "Licensing and Training")
- Depending on the complex, the type of letting will be either permanent (long-term) letting or holiday (short-stay) letting.

Despite having had three management rights operations before, we would never have got to where we are now (in this partnership) without Mark.

It takes a special person to be able to broker a deal between banks, lawyers and potential partners – and to sell us, as complete strangers, to them, as successfully as Mark has, and it speaks volumes about him and how he conducts his business.

Graham and Mel Young, Catalina



Management rights has six main elements

Onsite Manager

Body Corporate

Contracts for the caretaking of the common areas and letting of units exist between the body corporate and unit manager

Body Corporate Manager

Represents the body corporate (in some cases)

Committee

Representatives of lot owners within the complex

Lot Owners

Onsite manager holds contracts (Form 6) with investors/lot owners for the letting of units on their behalf and receives a percentage of the income

Real Estate

Ownership of a property in the complex – usually referred to as the manager's unit

Tenants/Guests

Onsite manager has a duty of care for residents and may earn additional income for the provision of predetermined services

Financial considerations

How much can I borrow?

- Up to 70% with no additional security
- Up to 100% with additional security
- Multiply your cash by 2.7x times to establish your purchase price
- Interest Only options – up to 3 years
- Redraw & Offset Loan options available
- 6% of the purchase price is a general rule for your upfront costs to cover –Stamp Duty, Solicitor, Bank, Accountant, License etc.

An example of a management rights purchase (based on a price $1million)

Unit	$400,000
Rights	$600,000
Sub-total	$1,000,000
Costs	$60,000
Sub-total	$1,060,000
Less Cash	$360,000
Funding	$700,000
On a building of this size, the net operating profit would be approx.	$120,000
Repayments on interest only would be approx	$34,000
Surplus	$86,000

From the above surplus, you would still need to cover your general living costs, tax, rates and levies

Comparison of cash purchase against borrowings and cash input of $450,000

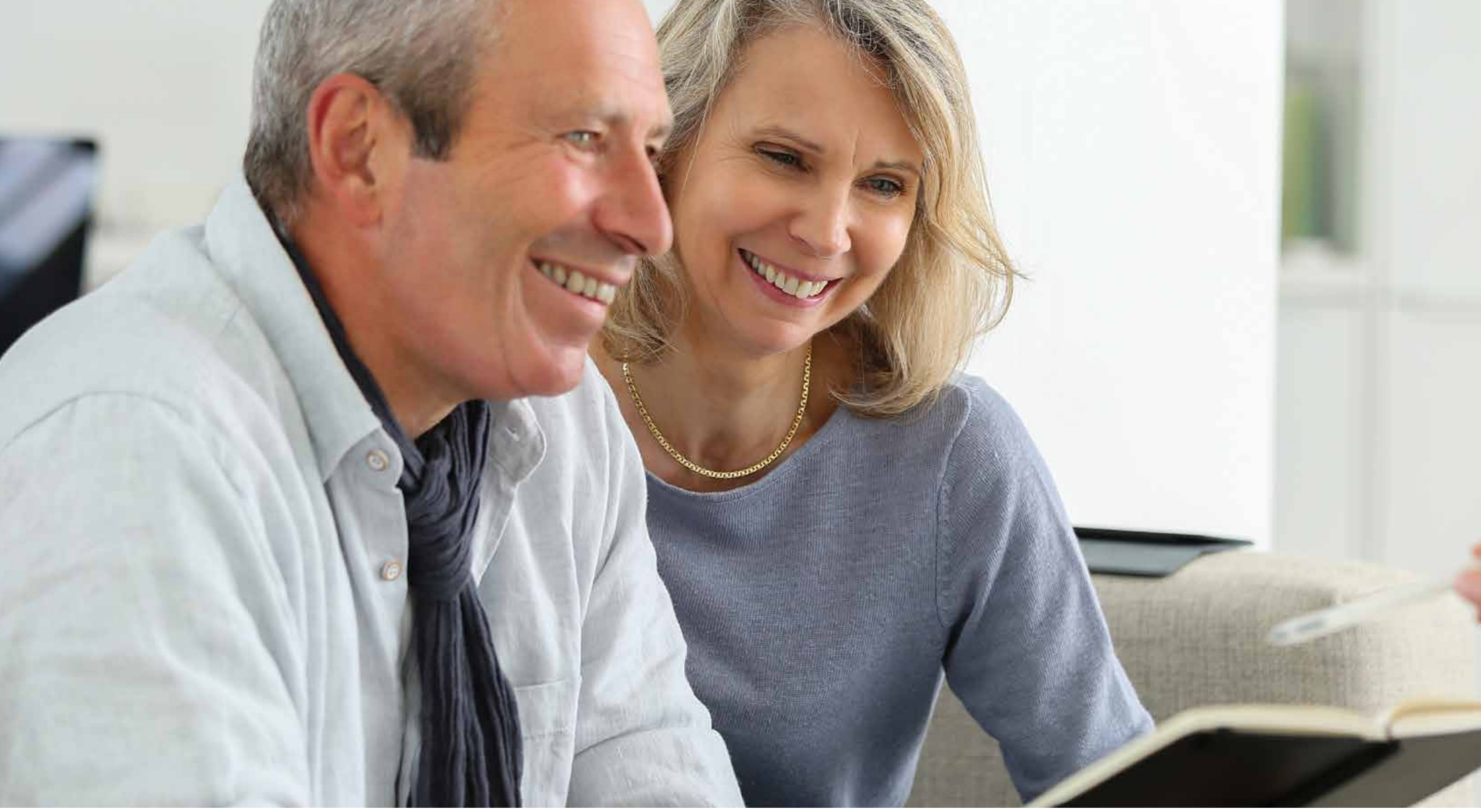
Contributing $450,000 cash with no borrowings	
Unit Value	$250,000
Business Value	$180,000
Costs	$20,000
Total	$450,000
Less Cash	
Income (factor 3x)	$65,000
Less Interest on Loan	Nil
Less Tax (approx)	$5,000
Net Income	$55,000

Borrowings + Cash Input of $450,000 to purchase a larger complex	
Unit Value	$350,000
Business Value	$850,000
Costs	$65,000
Total	$1,265,000
Less Cash	$450,000
Borrowings	$815,000
Net Operating Profit	$180,000
Less Repayments	$47,000
Less Tax	$25,000
Surplus	$108,000

Comparison of borrowing against property compared to borrowing with cash input

Borrowing against other property	
House $400,000 x 80%	$320,000
Plus Borrowing Against Complex	$450,000
Costs	$38,000
Total	$808,000
Net Operating Profit	$95,000
Plus New Rental Income	$13,000
Less Total Loan Repayments	$69,000
Surplus	$39,000

Cash input of $400,000 + borrowings of $600,000	
Cash	$400,000
Borrowings	$600,000
Costs	$50,000
Total	$1,050,000
Net Operating Profit	$132,000
Less Total Loan Repayments	$47,000
Surplus	$108,000



Buying into management rights – what else you should know

If you are considering the purchase of a management rights business you should allow a minimum of six percent of the purchase price to cover the following upfront costs:

- Valuations
- Accounting fees including financial due diligence,
- Legal fees including legal due diligence
- The registration and set up of a new entity (trust / company)
- Stamp duty
- Software changeover
- Training course to obtain license
- License fees through Office of Fair Trading
- Insurances
- Bank set up fees

Important: It is important to have a buffer and/or additional working capital ($10,000 - $20,000) available to run the complex initially until you start receiving the body corporate salary and profits. During the first month you might have to pay for cleaning, linen, wages and so on before you start receiving an income to cover these costs.

Levies

Each lot owner (including the onsite manager) pays levies that are managed by the body corporate manager. These levies are split between the administration fund and sinking fund, and will be disclosed by the sales broker and your lawyer.

Finance

Lending for management rights ranges between 60 – 70 percent depending on the following:

- Type of complex
- Experience of the purchaser
- Term of the agreements
- Level of income from the business and external sources
- Location
- Value of real estate

On a standard or accomodation module management rights, lending of 70 percent can be achieved.

The financier will normally provide two loans (depending on the amount and structure). The first loan is 80 percent of the market value of the managers unit and the second loan will be for the balance of funding required (business value).

Note: Interest only terms are available with some financiers while others require principal and interest on loan from commencement.

Management rights – Income potential

As one will appreciate, every building and management rights agreement is different and the income potential is largely dependent on the type of complex, location, size and schedule of duties agreed upon.

Types of management rights

Permanent property

Irrespective of whether this is a townhouse, villa or high-rise complex, a 'permanent' or 'long-term' property is one comprised of tenancies that are all long-term (minimum three months, normally six to 12 months leases).

The property by-laws prohibit holiday or short-stay letting, and the tenancies are largely governed by the Residential Tenancy Authority (RTA).

In terms of the management rights, there is minimal marketing required and the working hours and potential annual income is more stable.

Holiday or short-stay property

Predominately located in high tourism areas and open seven days a week, 'holiday' or 'short-stay' properties are comprised of 'investor-owned' units (or apartments) within the letting pool that are rented for short periods ranging from a single night to a maximum of three months, primarily to holiday guests. Facilities are resort-like and there is a strong emphasis on marketing and garden and facility upkeep.

A higher level of service is required for guests and revenue can be seasonal.

Mixed-use property

As the name infers, a 'mixed-use' property is a building that offers a combination of permanent and holiday rentals. This property may range from a small three-storey walk up to a large high-rise featuring resort-style facilities.

A mixed letting pool offers pros and cons as the residential manager needs to be able to effectively manage the divergent requirements of the different residents. Income potential is typically higher in a mixed-use property.

Corporate complex

A 'corporate complex' is typically located in established CBD locations, and is similar to that of a short-stay property. Tailored towards overnight to seven day-stays for travelling guests, additional facilities may include a dedicated business centre, function rooms and specialist services such as shuttles.

Dedicated marketing is required to attract guests and returns can be seasonal.

Student accommodation

Designed primarily to accommodate students living a university or other education facility, 'student' apartments are rented by the room or the entire unit. Rentals typically coincide with the term of the semester and/or duration of the study period (several years). Many of these rentals are made to international students.

Income potential

Body corporate salary

The body corporate salary is the agreed amount paid each month (in arrears) to the appointed resident manager from the administration fund on behalf of the lot owners. The salary is paid to compensate the resident manager for undertaking the prescribed caretaking duties within the complex/property, such as cleaning and maintaining all common areas, the cleaning and testing of pools and spas, the cleaning and maintenance of barbecue and entertainment areas, gardening and mowing, general maintenance and the supervision of trade contractors, building compliance and work, health and safety requirements.

Industry specialist

Permanent

An onsite manager receives an agreed monthly salary from the body corporate to maintain the common area and look after the complex. The salary is linked to the number of units in the complex and the duties involved, as detailed in the caretaking agreement.

As a guide, the average body corporate salary is around $1200 - $2,000 per lot in the property, therefore if you had 70 units in the complex, the salary would be between $84,000 - $140,000.

Additional income may include:

Commission: Typically based on 7.5 percent plus GST of the rent paid by the tenant

Letting and re-letting pool: Charged to the investor for sourcing, and maintaining tenants

Gardening and mowing: Charged to the investor to maintain the backyards of each lot

Repairs and maintenance: Charged to the investor to repair and replace items in the lot (eg: broken dishwasher / minor painting)

Short-Stay

The onsite manager receives a monthly salary from the body corporate to maintain the common area and look after the complex. The salary is linked to the number of units in the complex and the duties involved, as detailed in the caretaking agreement. As a short-stay or holiday property, it is likely that there will be more facilities in a holiday complex than a permanent complex, such as tennis courts, barbecue areas, saunas and recreational areas.

Additional income may include:

Commission of the tariff: (Usually around 12.5 percent + GST) to rent out apartments / rooms on behalf of the investor. A higher commission is charged, due to the higher volume of work required.

Marketing: A fee (usually around 3 percent) is charged for the active marketing of the property to local and international audiences.

Cleaning and linen services: The onsite manager manages the housekeeping and provision of linen providers on a daily, mid-service, or upon departure basis. The frequency of cleaning and linen depends on the type of complex and length of stay.

Tours and Transport: The onsite manager can arrange tours and transport to most tourism attractions.

PABX/Internet and cable TV: A monthly fee may be charged for the provision of telephones / wifi / Foxtel and/or Netflix for resident usage.

Repairs and maintenance: Charged to the investor to repair and replace items in the lot (eg: broken dishwasher / minor painting). While this demographic may require additional supervision and management in terms of hours worked, further income potential exists through the provision and bundling of ancillary services such as electricity, internet and furniture packages.

Management rights – A new manager checklist

Structuring

Before signing a management rights purchase contract, it is important to consider what business structure will be the most suitable to operate the business. ie. The unit is registered in personal names as the principal place of residence in order to save stamp duty vs a family trust for asset protection and taxation benefits.

MRM Finance will provide comprehensive advice and guidance pertaining to all options, as well as discussing the implications of each and every aspect including asset protection, taxation affects, and the costs of administration to ensure that you will be fully informed before signing the contract. Professional advice should be sought from your lawyer and accountant.

Financial due diligence procedure

A full financial due diligence will need to be performed for both you and the financier prior to purchase. This should be completed by a specialised accountant with extensive industry knowledge who will attend the complex and validate the prior 12 months of operating income and expenses to determine the net operating profit.

Important: Using the services of a non-management rights accountant can result in the financier not accepting their reports, and for you, as the client, having to redo the investigation at your own cost.

MRM Finance has the experience and industry knowledge to be able to review the reports produced by your accountant and to provide an accurate overview of the operation. A thorough due diligence report will detail all findings and will also provide valuable information to the purchaser regarding the commercial business operation.

Note: The financial due diligence is for the last 12 months of operations, and not a due diligence on the vendors tax returns.

Legal due diligence procedure

When purchasing a management rights business, you will need to engage a specialised lawyer to undertake the legal due diligence on the agreements.

The lawyer will review the agreements, by laws, history of the building and provide you with a comprehensive report outlining their findings. In most cases, this report will be required by the financier.

Note: As with the financial due diligence, it is imperative that you engage a legal firm with specialised experience in the management rights industry so as to ensure that all legal aspects of your agreements are valid.

Banking

The bank providing the finance for the management rights purchase will typically require you to establish the required trust account and general account through them. They will also establish internet banking services for you to access all accounts, and allow you to pay owners each month from the trust account.

In addition to these services, you will need to set up merchant facilities, to provide a facility for guests to pay for accommodation or services via credit card.

Trust account

The financier will require a copy of the Office of Fair Trading application / certificate to open a trust account (See information under Licensing and training).

The trust account is used for payments received from guests and tenants paying for accommodation or services that are held on behalf of owners/ investors, and distributed to owners during the first week of each month.

The trust account must be audited three times a year by a certified auditor, and the certificate must be supplied to the Office of Fair Trading each year.

Trust account software

There are various software packages to assist with operating the trust account that will effectively manage:

- Receipts of payments from guests and tenants
- Calculates amount of payment to the owner
- Calculates amount of payment to the onsite manager
- Three-way balancing
- Deposits held
- Owners ledger
- Tenants ledger
- Owners summary reports
- Overdue payments

Finance covenants

Financial covenants will normally be required by the bank with their finance approval. These covenants can include:

- Provision of letting pool numbers quarterly or yearly
- Provision of financial / taxation returns (annually)
- Ratio of profit vs income
- Completion of audit certificates
- Provision of taxation obligations
- Copy of insurance policies (public liability)

Licensing and training

Entry and involvement in the management rights industry, and the operation of a trust account, is governed by the statutory requirement of having a Resident Letting Agents (RLA), or full real estate agents license.

In Queensland an RLA covers a minimum of six units of competency that takes at least four full days in class or up to three months online. A full real estate agents license is comprised of 19 units and one of these units involves attending an auction.

Following the completion of the training course, you will receive a certificate of attainment, that needs to be lodged with the application to the Office of Fair Trading. The course and submission of the license application needs to be completed and submitted prior to settlement.

The appropriate auditor will need to sign/complete the Auditors Declaration section.

Operational and compliance training in building management and caretaking is also available through Australian Building Management Accreditation (ABMA) Building Management Code or ARAMA Management Rights Industry Training Program (MRITP).

To sum it up...

We've all heard the saying. 'knowledge is power.' This is truer than you can ever imagine in the management rights industry. Gaining knowledge upfront will help you to set up, manage and control your business from day one.

Consult and surround yourself with the right people and you will be able to establish a business that enhances the experiences of your owners, guests and residents. And when it's time to exit, you will have a highly desirable management rights business that commands top offers.

Next steps

To contact Mark Ryall with regard to a management rights opportunity or to discuss a review of your own personal financial assessment at no cost, please contact Mark on 0419 640 215 or mark@mrmfinance.com.au.

We look forward to working with you.

mrmfinance
Management Rights & Motel Finance Pty Ltd

To find out more contact Mark Ryall 0419 640 215
mark@mrmfinance.com.au | www.mrmfinance.com.au