mikephippsfinance

# 10 Urban Myths of Management Rights Finance

You may recall last month I mentioned finance myths in the context of 10 year agreements and standard module buildings. In a continuation of the theme here's the current Top 10 including a recap of last month:

**10 year agreements** - The banks don't like them, the banks won't fund them. That's nonsense. Certainly some banks pick and choose their lending and tend to avoid certain types of transactions. Having said that we are having no problem funding Standard Module management rights on competitive terms. Granted some smaller buildings can't carry 70% gearing but that's not to say they can't be funded. They can, just at a marginally lower gearing ratio.

**Interest Only on Standard Module** – You can't get interest only on ten year agreements. Not so, Interest only can be available. You do need to top up regularly and ensure your funding structure is well thought out.

**Valuations** - The banks tell the valuers what to write. The banks don't tell the valuers what to say. Valuers must be independent of the banks and they must use comparable sales evidence combined with an analysis of market trends to determine value. The banks do review valuations and if they feel the valuer has had a shocker they can reject the report and request amendments. Not something I have seen in the management rights sector due to the experience of the industry valuers. Of course, the manner in which a bank instructs a valuer can have an influence on the valuation outcome in terms of content and commentary but not generally on the dollar value arrived at in the report.

**Multiples** - The banks have secret multiple ceilings that they won't lend past. The banks don't have pre - set multiple tolerances. They do have levels at which a valuation is automatically required but they don't call the shots on multiples, the market does that. If a punter wants to pay over the odds for a business that's fine. Provided debt servicing works the bank will lend you the usual gearing against purchase price or valuation, whichever is the lesser. Just means that the buyer has to put up ore equity or security.

**Personal Guarantees and Asset Protection** - I don't need to put up my personal guarantee. Yes, you need to put them up. Sometimes limited when a partnership is purchasing. Usually limited to percentage shareholding of each individual. If you are borrowing 70% and don't want to guarantee your debt I suspect it says something about your confidence in your prospects for success. When discussing asset protection with your lawyer and accountant that's protection from litigation. There is no protection from your bank as a first ranked secured creditor.

**Lower Rates in Company Name with Residential Security** - The banks charge high rates for loans in company names. Not necessarily so, you can get a lower rate against property security and still have a business loan in a company name. If your bank tells you they are charging a higher rate because of the borrowing entity go somewhere else or call us.

**Paying Off Debt Early and Penalties** - I will get penalised if I make extra payments. Not always the case, you just need to plan ahead and set up your finance accordingly. Variable rates are best for extra repayments without penalties although it is possible to fix with a lump sum reduction plan. You can also park funds and redraw or offset. Remember, redrawing may create a part non tax deductible debt. Check with your accountant.

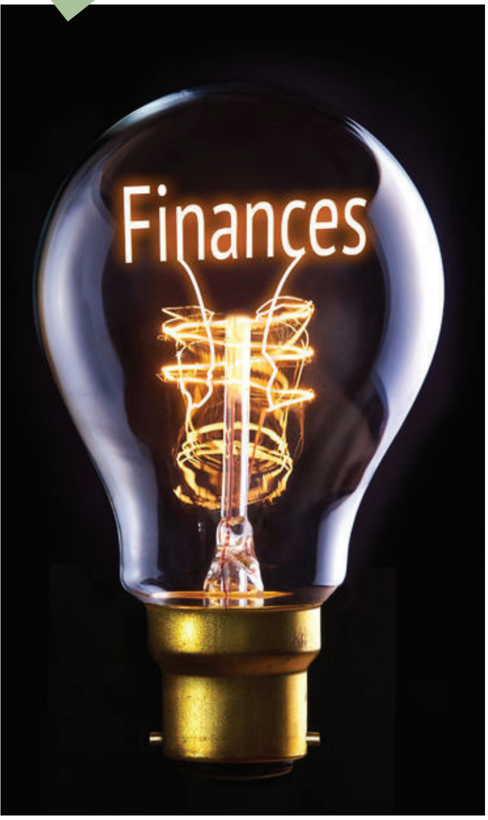
**SMSF Policy** - My accountant says I can borrow via my SMSF. Despite what your accountant or financial planner says the banks are not huge fans of SMSF lending for specialised assets. This includes motels and management rights. Not impossible in some instances but not the easiest transactions to set. Banks are terrified of APRA and ASIC surveillance of SMSF lending activity. Just because it's legal doesn't mean the bank will lend you the dough. Try funding a licensed brothel and you'll see what I mean.

**My Bank Will Definitely Extend My Two Year Loan Term** - Your bank is under no obligation to extend your loan past its documented term expiry date. If your letter of offer says 2 years then technically your loan is due in full at the end of 2 years. Banks strike short lending periods because short wholesale money is cheap and they can pass on the interest savings. Beware the expired loan term. If, in 2 years' time, your bank wants out of the management sector then you will need to refinance. Of course, banking professionals can structure finance to take advantage of the cheap money that short loan terms offer while ensuring debt roll over protection for the borrower. No, I'm not going to tell you how, that's a secret we only share with our clients.

**Banks Offer Cheap Rates and Then Put Them Up** - Interest rate pricing is determined by the RBA cash rate, The Bank Bill Swap Rate, the client risk margin or line fee and most importantly by competitive pressure. The banks can't do much about the cash rate or BBSW but competition between the banks means lifting existing client margins is a very risky strategy. If your rate goes up it will most likely be because the base rates have moved or your bank has repriced you because of a change in your risk profile. Typically repricing upward can result from being slack with requests for updated info from your lender or defaulting on payments. In my experience when banks offer cheap rates and are looking to improve their returns they tinker with fees. Be ever vigilant and keep an eye on your bank statements.

And number 11.......refinancing is just too hard and too expensive. Not necessarily so. Ask us how.

*PS : Our little company has been going for 5 years now.*
*We have enjoyed tremendous support from the industry and hopefully we will still be around in another 5 years.*

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