Off The Plan

Management Rights FAQs

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Off The Plan Management Rights - FAQs

What exactly am I buying?

Purchasing a management rights off the plan simply means that you are agreeing to purchase a management rights business and usually a managers unit at a future time once the project is complete and individual unit sales have settled. Off plans can be holiday resorts, permanent rental townhouse or unit complexes or short stay corporate properties like hotels and serviced apartments.

How do I know what I am buying?

The sale of off plan management rights is a highly regimented process and contract conditions are designed to ensure that the buyer is protected. Most importantly the sale will most likely be subject to claw back and claw forward conditions. Remember, in all likelihood the developer doesn't know exactly what he has sold until all the units are settled and the buyers have made a final decision about using your letting services. In most cases this process can take several months after completion. To protect all parties there are usually a number of settlements known as the initial settlement and the adjustment settlements. At the initial settlement you pay for what the developer delivers. Typically this will be the managers unit / office and the letting appointments so far signed by individual investors in the building. At each future adjustment date (usually at 3, 6 and possibly 9 months) you pay for the extra units the developer has introduced to your letting pool. Claw back and claw forward conditions are designed to ensure that you pay for what you get when you get it.

Sounds complicated. How do I manage my finance and how does the developer know I will pay for the units I gain after the initial settlement?

The purchase and finance process is specialised and requires a level of specific expertise. It is essential that you deal with an agent, financier, lawyer and accountant with experience in these type of transactions. We manage the finance process for our clients and work with their agent, lawyer and accountant to ensure we achieve an appropriate outcome. In most cases the developer will require a bank guarantee covering your obligations after the initial settlement. We will arrange this facility as part of your funding package.

How much will the banks usually lend?

As a start-up venture the banks see off plan management rights as a bit riskier than an established rights. Having said that available gearing ratios for off plans are still higher than just about any other sort of going concern start up finance. Available lending varies but generally you can look at 60% to 65% against the combined value of the unit and rights. Buyers with previous experience are more likely to obtain higher gearing. Remember, the GST can be funded on top of the core bank lending and is not taken into account in the gearing ratios.

Who decides how much each letting appointment is worth?

There is a specific calculation to arrive at the value of a letting appointment. It involves the expected net profit for the business exclusive of the body corporate salary. Opinions differ on the mechanics of the calculations although we all seem to arrive at approximately the same number. We recommend discussing the detail with your agent and lawyer as part of the contract negotiations.

Do I need previous experience?

For very large scale projects the short answer is yes. The banks will look at your business background and qualifications and make a judgement call on your capacity to take the business from start up to successful going concern. For most off plan management rights bank finance is readily available to applicants with appropriate skills outside the accommodation sector. A business plan outlining your strategies is always a good idea.

What should I expect to see from the vendor?

Ideally the vendor or the vendor's agent will present you with a detailed Information Memorandum supported by a projected profit and loss report prepared by an industry expert accountant. The report should reflect the anticipated letting pool numbers, expected occupancies and market rental averages. Supporting information such as marketing material relating to the project is always handy as is information about current demand for the project and the likely typical unit buyer profile. Remember, your contract will stipulate that you have your own accountant review the projections and proposed net profit figures. This, together with the bank valuation and approval process adds a significant degree of protection for buyers.

How soon should I get involved with the developer?

As soon as possible. It makes good sense to work with the agent, developer and the project marketers to ensure the best possible outcome for all concerned.

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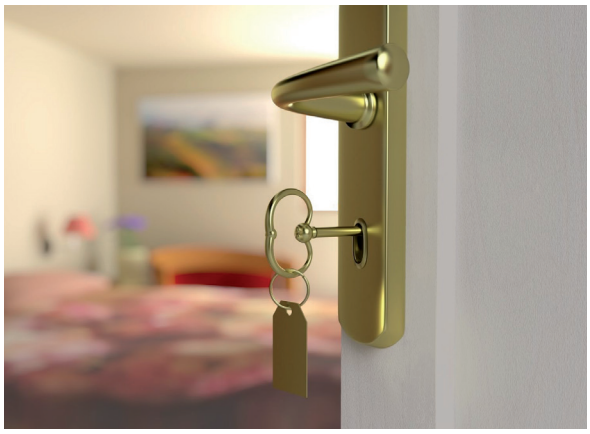

What if the project never gets off the ground?

Your contract should contain a sunset clause. Basically this is a clause that automatically gives you the right to terminate if the developer has not delivered the project by a certain date. Remember, it's a good idea to also think about sunset clauses for multi stage developments. You may settle on stage 1 and stage 2 never gets built. You don't want to be committed forever.

When do I put my money in?

Your equity goes in first and the bank lending comes in after that. We look at the claw forward and claw back arrangements, calculate how much you will need to complete your maximum contractual obligation, how much the bank will lend you and the difference is your equity. It's important to note that regardless of the likely final purchase obligation the strict contract conditions apply. This means that if you think you will get 80% of the units in the pool but the contract has no maximum stipulation we need to ensure we have sufficient finance in place to cover the unlikely event that 100% of the units end up in your letting pool during the adjustment period.

Do I pay Stamp Duty on the business?

Some good news here. In Queensland stamp duty is not payable provided you get your contracts right. However, you do pay GST. We can set up a GST facility for you with the bank and you clear it after you lodge your first BAS and get your GST back. The GST facility is treated separately to your other loans and is not taken into consideration in the banks gearing calculations.

The developer is using project marketers. How do I work with the developer and the marketers?

From the outset it is essential that you understand the developers marketing strategy and the role of any project marketers. Ideally the project marketers will not also have a property management function. If they do it is always wise to ensure that the marketers are not to offer property management services to buyers in your complex. If you are concerned ask the developer, agent or your lawyer about restriction of trade provisions that would prevent the project marketers from offering letting services to buyers either now or in the future. If you are buying into a mixed use development with commercial, retail or office space it's also a good idea to talk to the developer about proposed uses of that space. Ideally you don't want a real estate agency operating a property management business from your building.

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What if we get to the initial settlement and the developer has sold most of the units to owner occupiers?

Most specialist lawyers will suggest having a minimum letting pool provision in the contract. If the developer appears unlikely to be able to deliver a meaningful and viable letting pool you can decide to terminate the contract. Your bank will be particularly interested in this contract provision. Many specialist lawyers are also suggesting that contracts reflect the moving target that can sometimes be the challenge with off plan rights. That is, the contracts contemplate a variety of letting pool numbers and a commensurate variety of possible total management rights end values and individual letting appointment values.

It looks like the developer will want to put some of his units into the letting pool. How will these be treated?

Ideally developer lots (and those owned by associates of the developer) are excluded from clawback calculations. You should only be paying for those lots for which the owners intend to keep them in your letting pool for the long term. Remember that concentration of ownership / control of units in your letting pool adds a degree of risk that the banks are not keen on.

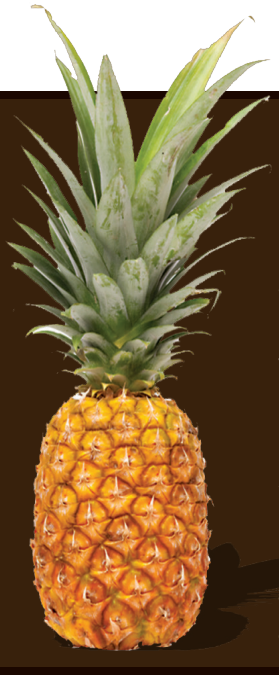
Settlement is in 6 months' time but I need a finance approval within 30 days. Will my valuation and finance approval still be valid in 6 months?

Banks approve finance on the basis of the approval being good for 90 days. If your initial settlement is within that time frame then your loan has commenced (even if not fully drawn) and all is well. If your initial settlement is more than 90 days after the issue and acceptance of the banks Letter of Offer then theoretically your finance offer has expired. The practical application is that the bank will approve the finance predicated on a valuation done at the time of approval and will extend that approval as and when required. Occasionally if the initial settlement is not expected for an extended period of time the bank may approve the finance and have a valuation done closer to the settlement date. Short of a catastrophic financial or legal disaster in your life the risk of your bank failing to re-confirm your finance post 90 days is considered very low.

What happens if I pay for a letting appointment and then lose it during the adjustment period?

This is an inherent business risk for any off the plan purchase, but also for any existing management rights business. Under law, a letting appointment can be terminated on 30 days' notice by either party at any time. Remember that provided you get your contract right letting appointments you win after the initial settlement from buyers who did not initially commit to you are yours free and clear. In this situation you only pay for letting appointments delivered by the developer. Equally, if the developer hands over an appointment and you lose it the general wisdom is that this is not the developer's problem. Basically it's a bit of give and take either way.

Please be aware that purchasing off plan management rights is a process best undertaken in conjunction with industry experts. The content of this FAQ is simply designed to give first time off plan purchasers a very basic idea of how the process works and what may lie ahead. We are happy to put you in touch with specialists in sales, law and accounting who can assist you to better understand these opportunities.



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