Negotiating the purchase of a commercial property

Greville Pabst is CEO of WBP Property Group, one of Australia's largest independently owned and operated valuation and property services companies. WBP Property helps clients make informed decisions when buying, selling and managing residential and commercial real estate.

WBP's highly skilled and independent valuers, advisers and managers work with the mortgage and finance industry and its clients.

Negotiating the purchase of a commercial asset is a tricky business. There is much to consider, including:

- How much should you pay?
- Is the yield commensurate with the wider market?
- Does the property have tenancy in place?
- What are the leasing terms?

To some potential buyers these considerations may be cause for anxiety. For an expert negotiator they are simply opportunities to negotiate a better purchase outcome.

When tackling tricky negotiations there are some key points to consider. You may then use the resulting information to achieve more favourable purchase terms or even a lower purchase price. These points include:

What type of commercial property is right for you?

This is the first question you should ask. The answer will be dependent on your goals. Some commercial properties offer significant depreciation opportunities on plant and equipment. Many property owners use these to offset taxable income. Other properties may offer strong returns and are purchased on the basis of rental income.

Understanding your investment requirement will make the search for a commercial property much easier and allow for a more strategic approach to negotiations.

Historical performance

Always undertake independent research and investigate the historical performance of both the commercial asset and similar properties in the area. Assess the property performance over several years (if available) including capital growth and yield. Are your findings consistent with the advertised yields? Discrepancy may provide room to negotiate.

> **Greater information may allow for a more strategic approach to negotiations.**

Leasing

Analyse the leasing documentation for any pending or outstanding lease renewals. Some leases may be nearing the end of their agreement with the onus on you or your property manager to find new tenants or manage the renewal. Some tenancies, such as major supermarkets, underpin the success of an asset and should be considered when reviewing lease documentation.

Also review the payment history of tenants. If there are payments in arrears this could indicate poor management and/or poor tenant quality that could create difficulties when you take ownership of the asset. Negotiate with the current owner to collect or settle outstanding debts or account for this in the purchase price.

Rents

Is rent commensurate with the market rate? It is important to set a fair and reasonable rent that reflects the sector, geographic area, size and fit out of the property. If rents are out of step, does the agreement allow for a rental review or is the lease nearing completion allowing you to adjust it?

In some instances a tenant may pay a higher rent in order to repay a fit out funded by the landlord. If the tenant terminates or doesn't renew the lease does the lease stipulate the tenant must reimburse the landlord for the expense?

High rent may warrant further investigation to ensure you are not met with any post-settlement surprises that may impact the asset's ongoing viability.

Hidden costs

Are there any additional operating or maintenance costs associated with the previous owner or tenants that could impact your future ownership and returns? For example, site contamination such as that from a service station may require specialist treatment or disposal at significant expense.

Consider potential future costs and either negotiate these into the contract, have the owner remove it prior to settlement or negotiate with the tenant to dispose of waste.

Fit out

Check the condition of the existing fit out of the property. If it is in poor condition or in need of a new fit out is there provision for this in the lease agreement? You should include terms regarding a new fit out every few years to ensure the property is maintained to a quality standard.

If a property looks dated review the leasing terms to check if a fit out is included and whether it has been enforced. Also investigate whether the tenant has contributed funds to the fit out. In this case part ownership should be registered in the lease documentation.

It is important to research each of these key areas before purchasing a commercial property to ensure you buy an asset and not a liability.

If you are considering a commercial property for your business or your portfolio remember to contact our office to assist with your finance options.