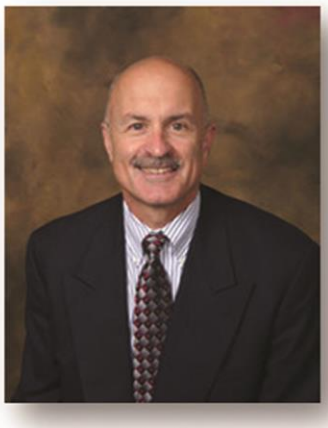
12 SECRETS OF SUCCESSFUL COMMERCIAL PROPERTY OWNERSHIP



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2014 is definitely a year for you to determine how to Stop Leasing and Own your business property!

In this report, you'll find 12 Secrets on how to begin and maneuver the quest for the right commercial property for your company.

COLDWELL BANKER COMMERCIAL

They do me wrong,
Who say I come no more for every day,
I stand outside your door...
Opportunity

Walter Malone 1903

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The 12 Secrets of Successful Commercial Property Ownership

Summary

If you've come to a place in the operation of your business where you have begun to consider the acquisition of a commercial property or building, Congratulations! There are some tremendous advantages in ownership of your business property, and many companies have included ownership as a very key piece of their overall business strategy.

As with any major business undertaking, this is a great stage to clarify the vision of where your business is headed over the next several years. Possibly, updating your business plan and ensuring that this path provides the best return on the allocation of your time and resources. While there is much to do to bring the correct resources together to move forward, it is very achievable.

Begin to build a team of professionals who can help you put those resources in place. Your CPA and attorney are great places to start. Finding a commercial realtor who understands what you're looking for will be an important addition.

These three can assist you in gathering data to begin creating a plan, developing a budget, assembling information on prospective properties and sifting through the challenging world of commercial lending with the range of options you will face there. They can help provide step by step guidance in coming to agreement with a potential seller, and then finalizing the transaction.

Advantages

There are a number of advantages to owning a commercial property. The primary advantage being, building *Equity*. In other words, *Building Wealth* or *Growing an Asset*. As you go through the process, keeping this thought uppermost in your mind will prove to be the key to reaching your goals. You will find there is a great need to devote a fair amount of time and resources to seeing it through to completion. A second advantage is providing a more stable fixed cost/overhead situation for your business to operate in the future. As a general guideline, business becomes more expensive to operate each year. Increasing lease rates, inflation, regulation, taxes and health care costs all have an impact. Real estate costs are usually the 3rd or 4th largest expense to any business. Stabilizing real estate expenses can improve your cash flow, make you more profitable and provide a competitive advantage in the future.

1 Clarify Your Vision

Let's get right to the heart of the matter, what is your objective in owning commercial Real Estate? Is this really the right business decision for you and your company at this point in time? Is your business truly doing so well that you are confident of being in business five years down the road? What major business roadblocks do you see within the next couple of years? Do you anticipate any major growth spurts that could impact your space needs?

As a general guideline, building equity (wealth) is the primary reason to buy, instead of lease your commercial property. Let's be real. You have worked hard to build your business into a "platform" that helps provide an income and is one that you enjoy. You've already built "equity" there. Perhaps it is time to determine whether you can harness the financial power of the monthly lease payment and create a second platform to generate additional wealth.

2 Update Your Business Plan

This is a good juncture in the history of your company to stop and review the road you have traveled. Take stock of what has been accomplished, and give thought to what your company will look like in five to ten years. Project your sales, staffing needs, equipment requirements, and space needs. You will find you gain many insights as to your true needs for business property. The Washington State Small Business Development Program, Score, and the US Small Business Association are excellent resources to help you with this step.

3 Exit Strategy

Owning your business property provides you with a greater range of options as you develop an exit strategy for your business. You may sell the business and the property together as a package. Perhaps you will sell your company and the new ownership will remain as a tenant, thus you move into the landlord and property management business. You will continue to generate income from the property, and have the equity grow. Your exit may be by an entity buying both the property and business together. Or you may decide to simply close your company and lease the space.

> **"Give me six hours to chop down a tree and I will spend the first four sharpening the axe."**
>
> ***- Abraham Lincoln***

4 Build Your Team

Knowledge is power. The more knowledge you can bring to bear in the process of acquiring your commercial property, the better decision you will make. However, you personally don't have to know everything. This is where putting together a powerful team of professionals, proficient in their areas of expertise, is really your first step.

We assume you already have an accountant, or CPA, as part of your team and you will want them to play a key role in this process. Prior to moving forward, they can help prepare the financial reports and information you'll need to provide your potential lenders. They may also be able to help you with future projections, and then incorporate the tax implications of these decisions into those projections

A second vital resource is a terrific commercial realtor. You want someone who is knowledgeable about the type of property you want to buy and has the ability to dedicate the time and resources to helping you find that perfect property. Be sure you select someone who you feel will fully listen to your aspirations.

In most cases, an attorney will play a pivotal role. Most real estate is purchased with a separate business entity than what you operate your company with and your attorney can help you with this. They can also clarify questions that many arise during the negotiation stage of the purchase and sale agreement, as well as assist you during the closing process with the Escrow Company.

Creating a relationship with a commercial lender will be a top priority. Choosing the lender and the financing program can be as important as the selection of the property itself (we'll discuss this in more detail in a later section). Certainly meet with your current bank representative, but use this occasion to expand your network.

A critical area, that is often overlooked, would be the Title Insurance Company. No real estate transaction is complete without the work they perform. They are the ones who insure that the title to the property is clear of any liens. They also oversee that all the correct documents are in place, signed properly, recorded with the local agencies in a timely manner, and distributed to the correct parties. It is this company's responsibility to search the chain of title on your specific property and make sure there are no defects that could prevent you from taking full ownership. Prior to the closing (which is the act of transferring of ownership from the seller to the buyer), the Title Company provides a preliminary title report that will list "exceptions" to taking full title. This simply means a list of possible claims that could be liens, or "special right of ways", that a government agency, utility or a neighbor might have.* Examining these reports is a critical part of your research. When completed, the company issues a policy, or "title insurance", that says they will stand behind their work and guarantee that when you purchase the property, nothing will jeopardize your title.

** some exceptions can be of a more serious nature.*

Areas that often get deferred, in the property acquisition process, are the government permitting process and cost of development or refurbishment. Above and beyond the actual materials costs, the "soft costs" can add up quickly and have a major effect.
You will want to hire a professional who has a background in the development process. Someone who can help evaluate how these costs and processes may affect the final expense of preparing the building for use. This may be a construction company who has hands on expertise with developing, or it may be a planning architectural firm.

5 Develop A Plan

The next logical step, after you've gathered your team, is to create a plan that lists the roles you want each team member to play. Including what you rely on them for and some time lines that will help ensure you are staying on track.

6 Rally Your Resources

Now, your team is ready to be put to work and help you gather information.

Your accountant can help gather your tax returns. Most lenders are going to require three years of tax information. This will include both the business and personal returns. They will also want you to do a personal financial statement and a balance sheet for your company, if it is going to occupy the building.

You can determine how much capital you have available for a down payment using guidelines from your lender on what the *Loan to Value Ratio* requirements are. This will help you determine the upper limits of what you might be able to purchase.

Your attorney can begin the process of setting up the proper documents for holding your property. It is a generally accepted standard that ownership of commercial property will be in a designated legal entity. Often, this is a Limited Liability Company (LLC), but there are other options to explore as well.

"I am working today in every way possible to protect this money from inflation. Commercial property is an excellent place to invest money for inflation protection..."

- Les Schwab, "Pride in Performance: Keep it Going"

7 Run Your Numbers

Create a Budget

This is a critical step. It is crucial that you create a budget for both the acquisition of the property and for the business operation. Don't skimp on this step. It is actually one of the very first steps you should take as you assemble your team and get their feedback on your work. This can dovetail with the major review of your entire business model and plan

Compare Operating Expenses

Run projections on your current operation and create a scenario of what your company might look like after your building purchase. Are there costs that change? Do they affect the profit ratios within your business? Utilities, landscaping, maintenance and insurance may be quite different in your new set up. Will the new business model have the sales to support these expenses?

Moving expenses

Often times this expense does not get considered until after the purchase has been completed and the next step is time to move. Moving can be expensive in both time and actual cash outlay. Incorporate this into some aspect of your preparation.

8 What Is The Best Return On Your Capital?

Two key elements of successful businesses are cash flow, and working capital. Purchasing a building can have a tremendous impact on either or both. Purchasing a property will require some level of down payment and it is a commitment to tie up some of your hard earned capital. This may be capital that you are holding within the company, wanting to put it to work. It may be personal capital you have that is outside the company, perhaps invested in other vehicles. If you are expanding, purchasing newer updated equipment may be part of the mix.

Either way, you are making a choice as to how best to employ your capital for the future. You should consider if investing in the building will give you a better return than putting the money into stocks/bonds, or in the bank? What could you accomplish by purchasing another operation, or expanding with another product line?

Let's lay out one scenario, just for a benchmark, and we'll make it with easy round numbers so we can perhaps apply it to your situation.

You decide to purchase and refurbish a building. Your total purchase and improvement costs will be one million dollars. You use an SBA 504 program which requires you to put up only 10% of the project value, and borrow the balance. $100,000 in capital, $900,000 in loan. This enables you to have $100,000 in investment capital. Assume you stay in the building for 10 years, and have a loan term of 22.5 years at an interest rate of 5.3%. At the end of that period, your balance on the loan is roughly $657,000 dollars. You've created $243,000 in equity (wealth). That is a return on your invested capital of 13.2 %. Now 13.2% is certainly far superior to anything you can generate in the current banking environment. Even with average annual stock or bond market returns over the past decade! This scenario includes only the equity created by paying down the loan and it does not account for any increase in property value generated from inflation, or ongoing development within your community. Understandably, there may be other ways you could employ that capital within your company to generate a higher return and those options should certainly be explored.

We'll also put a disclaimer here that this is just a scenario. Each individual project will have its own specific down payment, loan amount, interest rate and payoff period. It also assumes the value of the building, after ten years, to at least equal your original project cost.

9 Do Your Research

You'll never have 100% perfect information, but a thorough use of available resources will help you put together a very complete package.

Demographics

Demographics can be obtained in a variety of sources. The US census bureau is a great beginning source. Results from the 2010 census are being released on a regular basis, and will include information on median age, household income, growth trends, education levels and distance from your office.

Location / Location / Location

Gather comparable property sales from other areas of your community, as well as within the 3 to 5 mile radius of your proposed location. For example, traffic flows of surrounding streets and lists of nearby competitors.

Keep your eyes open for news articles pertaining to the commercial real estate market. Where are the "hot" areas in your community? Do conditions favor buyers or sellers? What is the

> "Risk comes from not knowing what you're doing."
>
> - *Warren Buffet*

trend on interest rates? This information can be gathered both from local news sources and using the internet. Conducting a Google or Bing search for "commercial real estate trends" will give you results and resources that include national trends, analytics and market research.
You will also want to gather a history of what the vacancy rate has been over the past few years. What are the current levels? Have they been stable, or is there a change in the neighborhood that is causing them to increase? Talk to other business owners in the area. Drive around the three miles radius to get an overview. Obviously, the atmosphere and dynamics will be different if you are opening a dental office vs. a café or a fitness studio.

Access
How easy or difficult is it to access the property? Is it visible and easy to turn into? Even with today's technology, is it easy to explain how to drive there? What is parking availability? Is there a charge? Is this a new expense? Will it impact your ability to grow your revenues?

Competition
This may be considered your part to update in the Business Plan. Particular attention should be paid to this step.

In the Zone
Does the current zoning match your needs? If not how difficult and time consuming might it be to change? Zoning laws can regulate not only the type of business that can operate, but also access to parking, signage, appearance of the building, waste management, noise levels and disposal of storm water. Zoning guidelines are often affected by the laws made by state, federal and local government agencies. Your local city, or county, will have resources available on websites, as well as individuals within government development departments who are there to answer questions and provide some guidance.

This will be a critical step in the acquisition process. It is not a given, because a previous tenant or owner of a property was zoned for a specified use, that it will carry over to your use. If a property is zoned differently than your anticipated use, part of your due diligence will be to determine the length of time and expense required to bring it into compliance. The process can be long, arduous and costly. There may be more suitable properties that already meet your needs. This is an area where the members of your team; commercial realtor, contractor, and architect, will be of invaluable help.

Inspection
Prior to purchasing a commercial property, bring in your team of professionals to thoroughly examine the structure and the systems in place. Electrical, communication and internet, plumbing, heating and air conditioning (HVAC) are all components of an efficiently functioning building. This is another area where members of your team, contractor and architect, will provide a valuable service.

10 Meeting Of The Minds

This may sound like an oversimplification, but purchasing a commercial property is really just two parties coming to an agreement. It is that simple. But, it is not that easy. There can be a dozen or more small agreements needed to make up a larger picture. Having a clearly drafted purchase and sale agreement (PSA) is key in your commercial real estate deal. A PSA is required for you to place the deal in 'escrow' with your title company.

Each detail of the transaction will need to be documented:

- Legal description of the property
- Purchase price and any terms that might be involved
- Period of time allocated for due diligence or feasibility studies
- Can the period be extended and, if so, will there be a cost?
- Time periods allowed for financing and closing
- How will property taxes and utility bills be pro-rated between you and the seller
- What types of legal recourse is available if either the buyer or seller defaults

Your commercial realtor, as well as your attorney, will provide you support here. Many realtors work with standardized PSA templates approved for this specific legal transaction. It is always a good practice to have an attorney review a draft of the contract before you present an offer. They can provide additional insights and explanation of any legal jargon, and will they be able to respond more rapidly if any legal issues arise during the closing process. It will be your attorney who delivers final instructions for closing to the escrow agent at the title company.

11 Financing

Historically, the financing piece of commercial property transactions has been a critical element to any commercial property deal. Given the advent of the financial crises we experienced over the past several years, and the ongoing regulatory and management environment in the banking industry, lending remains a challenge. However, owner occupied properties are a preferred category for most financial institutions.

What this means for you, as a potential buyer of commercial real estate, is that you will need to lay a solid foundation in preparation for the lending process. We discussed earlier that one of the most valuable members of your team will be your accountant, or CPA. No matter what lending source you select to make application for a loan, you'll be asked for some standard

"What better to invest in than your future?"

- Patricia Rice

financial reports. Income and expense statements, often for three years, balance sheets and personal financial statements are required from any prospective owner(s) of the property. Often many business owners don't have very detailed copies of these reports. There is no reason to wait on preparing these, as they are valuable in so many ways.

Analyze your current situation. If you have followed the second step we listed above, doing a global review of your entire business plan, you'll be working from solid data. You'll be more confident when moving forward and will have a very clear picture of the level of financing you can afford, as you sift through the many prospective building acquisition options.

In addition, removing the stress of trying to provide these under a short financing time window is well worth the effort. Other documents you may be asked for could be; a profile of executive summary of the ownership group and business management team, an outline of how you plan to use the property, the Purchase and Sale Agreement and/or a property appraisal. These will all be part of a final package with your lender.

Source of Financing Options

While you will have a wide array of options, as you go through the "shopping" phase of looking for a commercial real estate loan, it will be beneficial for you to choose a lender early in the process. This will aide you in maximizing your leverage and getting the lowest cost on your funds. It is also very important to know how much you're qualified to borrow, as that will provide key information to your commercial real estate broker in determining the prospective properties available to you.

Several factors will determine the final rate you receive from your lender. Obviously, the existing financial market conditions at the time will have a primary impact on the rate. However, so will the anticipated use of your property, size and type of real estate and the lenders perceived risk of placing the money with you.

Each loan is tailored to the unique specifics of that situation. Certainly one place to start your search would be with your current bank or credit union. If you have a long term history with them, and they know and understand your business, the process can go relatively smooth. Just as with assembling your financial information, there is no reason not to start the process and strengthen your relationship with potential lenders, either your current providers or potential new partners.

Given the ongoing higher vacancy rates in the commercial property market, you may find it worthwhile to explore the idea of partnering with another company, investor or developer in a joint venture capacity. Possibly taking space in a vacant building, or partially completed project, and acquiring some equity. Keep in mind, these situations can be more complex and are not for everyone.

A term lenders and commercial realtors use to describe this type of use is "owner-occupied", or "owner-user". One upside on this type of use is that, even during the toughest months of the past couple years' financial crises, many institutions were still open to making loans to owner-users as lenders perceived the overall risk as being reduced. That trend continues today and

banks are very open to owner–user borrowers. Now, they may require you to also establish a full banking relationship with them, keeping the deposits of your business there to facilitate the loan. This is simply one more reason to do your research prior to identifying the property, so you can fully consider the implications.

12 Government Programs Designed To Promote Entrepreneur Development Of Property

The US Small Business Administration (SBA) is a great source of information, tools and loan programs for small companies looking to expand and/or purchase their commercial property. The SBA does not offer loans itself. However, it works through banks and non-bank lenders, known as Certified Development Companies, to help educate and execute lending.

Two of the primary programs the SBA uses are The SBA 7(a) program and the SBA 504 program. The SBA 7(a) program is the most commonly used. It is provided through both banks and non-bank lending institutions. To be eligible, you must be a for-profit business, and you cannot purchase real estate for investment purposes. Many of the guidelines for qualification have been adjusted, as part of the ongoing efforts to stimulate small business activity within our economy. All SBA 7(a) loans have prime based floating interest rates. These can leave you vulnerable to fluctuations in payment amounts in the future.

The SBA 504 program has a very specific goal at its heart. It is to provide a long term fixed rate loan base with a low down payment to assist small business in building or purchasing properties, in hopes of spurring growth in the local economy. Most loans under the 504 will be 10% down payment. There are some basic criteria you must meet to qualify for that 10% level. The other 90% of financing will come from two places. 1. Up to 50% of the total cost (building, land, renovations and soft costs) will be provided by a first position loan from a private-sector lender, bank, or credit union. 2. The other 40% will be a second position loan that will be provided by a certified development company. This portion of the loan (the 40%) is guaranteed by the SBA,

has a fixed rate of interest with a 20 year amortization period and it is assumable. This provides the borrower fixed payment rates for the life of the loan and great flexibility. Essentially, you have two separate loans ending up with a blended interest rate that is below market.

Most lending institutions require a range of 20 to 30 % for the down payment on a commercial real estate purchase and will not fold in the soft costs and closing fees. When understanding the combination of advantages available in the 504 program; lower interest rates, smaller down payments, inclusion of equipment and improvement lists into the loan, as well as fixed rates over a long term; participating in the program can translate into significantly lower monthly payments, which impacts your cash flow and ultimate bottom line.

> **"It's tangible, it's solid, it's beautiful, it's artistic, from my standpoint, I just love real estate."**
>
> ***- Donald Trump***

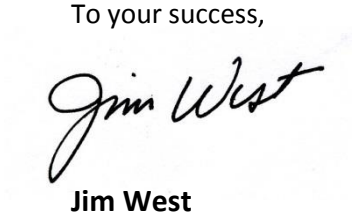
In summary, these 12 steps will help guide you on your journey to acquire your business property. Further, you have seen real-time examples in my workshop, "Commercial Property 101", of companies just like you who have successfully navigated the path.

It can be done.

It will take your willingness to put this knowledge into action and dedication to your goal.

Yes, you'll be investing some time and you'll need to make some adjustments along the way, but your team will keep you on the right track!

To your success,



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