

Due Diligence in Selecting Your Property: Assessing Business Financials & Valuation



Chuck Anderson

 *Marilyn Bushnell & Associates*

What is Value?

NOT Price:

Asking or Selling. One person's assessment of value.

NOT Cost:

Actual amount paid or actual cost to build or improve.

Value:

Defined as the power of a good or service to command other goods or services when exchanged in the marketplace.

Types of Value

Investment Value:

The value to a specific investor based on that investor's requirements.

Insurable Value:

The value of those parts that are physically destructible.

Assessed Value:

Value established by a tax assessor.

Liquidation Value:

The likely price that could be realized in a forced sale.

Fair Market Value

“The most probable price a property would bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus.” (The Appraisal Foundation)

1. *Both parties motivated, informed, acting in own self-interest.*
 - A. *“Arm’s length” transaction*
2. *Reasonable time for market exposure.*
3. *Payment in cash (not goats or shells!).*
4. *No unusual financing concessions.*

Gross Revenue Multiplier (GRM) – varies with the source

Sale or asking price ÷ gross revenues = GRM

Price is \$1,000,000 and room revenues are \$200,000

\$1,000,000 ÷ \$200,000 = 5.0 GRM (typical range for B&B is 3 – 6)

Price per Room (PPR) – generally not relevant for B&B

Sale or asking price ÷ number of rooms = price per room

Price is \$1,000,000; 10 rooms

\$1,000,000 ÷ 10 = \$100,000 per room

Asset Cost Approach (relevant for “Lifestyle” Inns and B&BS)

Value of real estate (as residence) plus one year's gross room revenue if revenues exceed value of trade fixtures (FF&E = furniture, fixtures, & equipment).

Income Capitalization Rate (CAP Rate)

Capitalization rate calculated by dividing NOI (net operating income) by the purchase price, usually expressed as a %.

Capitalization rates (on room revenue) for financially viable inns range between 8-11%. Typical target is 9.5%. Can go higher with restaurant.

Gross revenue = \$225,000; operating expenses = \$125,000; NOI = \$100,000

NOI ÷ cap rate = price (value?)

Cap rates and price are inverse:

\$100,000 ÷ 9% cap rate (.09) = \$1,111,111

\$100,000 ÷ 10% cap rate (.10) = \$1,000,000

\$100,000 ÷ 11% cap rate (.11) = \$909,091

Financial / Investment Analysis: Balancing Asset & Business Value

Can the Inn pay for itself? Will a bank finance it?



Key Factors Affecting Value: Location, Condition, Income, Local RE conditions

Key Factors Affecting Price: Motivation (on both sides), Lending

Get it right the first time and the rest will fall into place!

Due Diligence in Selecting Your Property: Location & Competitive Environment



Chris Kelly



What Type of Property Are You Looking For?

Existing Inn, Conversion or Purpose-Built

Where are your Guests Coming From?

Local v. International? New v. Repeat?

How Far away are you from Major Markets?

How Reliable are these Markets?

Where is the Property Located?

In-town? 5 Minute Drive? Address in a Neighboring Town or across a State Line?

How Do Guests Get There?

Is it a Fly-in, Boat In or Drive Market. Walk-In Traffic? Near Highways?

Is the Property the Destination?

If not, can it be? Is another Property the Destination?

Is the City, Town, Region or County a Draw?

How can the Property take Advantage of This?

Why Are Your Guests Coming To The Area?

Leisure Travel, Business, Family, Weddings, Groups, Corporate? How does the Property & its Amenities Support these Guests?

What Do I Look For On-Site?

Immediate Surroundings. Neighbors. Noise. Owner's Quarters.

Who is My Competition?

Visit and Compare these Other Properties as best you can

What Opportunities Does The Area Offer?

Is there more Growth Potential here?

Online Reputation & Competition

Research This Before You Go.

How Many Rooms? Can I Expand?

Can you Expand # of Rooms on Property? Is there Area Demand?

What are The Property Revenue Streams?

Room Sales, Weddings & Events, Dining, Spa, Groups, Wellness

Where do You Want to Live & Work?

Location Should Address Your Personal & Business Needs/Wants

What are your Personal Priorities & Passions?

Is the Property and/or Area Capable of Fulfilling these Needs

*Most importantly, Can this property and
Location Serve your Future Goals.*



ALP CONFERENCE & MARKETPLACE



Association
of Lodging
Professionals

Due Diligence in Selecting Your Property Inspections



Tim L Piper
Hearthside Group

Inspections



Due diligence is the key to your success and ultimate Return on Investment as a hospitality professional. Don't fall behind with a faulty inspection process.

Inspections help to determine the health of the property. Properties that need a lot of work are properties you don't need.

**Rule #1 – As a buyer, DO NOT fall in love with a building
But do find knowledgeable professionals to assist you.**

Rule #2 – Look for keys as to whether the property is well maintained.



- Here are some keys to maximize your inspections;
 - * Make sure there is an inspection contingency in your agreement
 - * Ask how long have they been on the market
 - * Review the financials... look at the maintenance expenses
 - * Ask for a list of all capital items in the last 5 years
 - * Speak with the owner as you view the property – get a feel – are inspections up to date? HVAC systems well marked, clean, accessible storage areas?
 - * Ask if there have been any code violations in the last 5 years
 - * Hire an inspector that specializes in hospitality or commercial properties
 - * Review the inspection with your professional inspector – prioritize issues if any

Then...

- * Once the inspection is done, determine if additional more detailed inspections are needed.
- * Ask if there are any “grandfathered” code violations; do they convey
- * Determine if there are any negotiable items beyond normal wear & tear

Remember – Inspections, when done properly, can get your career off to a great start focusing on the marketing and guests and NOT deferred maintenance

There's More...

- Spa permit requiring facility inspection and technicians licensed (typically by the state) to provide services
- Pool permit requiring inspection and regular water quality testing
May require lifeguard and or CPR certification as well as handicap accessibility equipment.
- Septic system inspection and approval by local or state health department.
Septic capacity whether private or public may limit the number of guest accommodations, dining seats and may limit future growth.
- Parking may not require a permit for on site parking but the local authority may require you to have a stated number of onsite parking spaces to accommodate guests, staff and owners, if in residence. This may limit future expansion if space is not available.

Due Diligence in Selecting Your Property Licensing and Permitting



Carol Edmondson

Inn Advisors





Licensing and Permitting

Due diligence is the key to your success and ultimate Return on Investment as a hospitality professional.

Whether and how a property can be licensed and permitted and by whom is a pivotal question. It changes with location and local authority, and often with a change of administration in an established local authority



Rule #1 – As a buyer, DO NOT fall in love with a building
But do find knowledgeable professionals to assist you.



Rule #2 – Assume nothing, do your homework and take your information directly from the licensing and permitting source.



What Are They?

- A variety of licenses and permits may be required to operate your business. Some examples are:
 - Lodging or innholders license/permit to operate and provide guest accommodations
 - May involve any or all of these local authorities, building, fire, health, zoning, historic (both local and state),
 - Food Service permit often requiring a ServSafe certification
 - Requires meeting the local/state health regulations and passing health dept inspection of kitchen, storage, refrigeration, ventilation and fire suppression systems
 - Liquor licensing – both state and local, full service vs. beer and/or wine
 - May be limited by availability of controlled # of licenses.

There's More...

- Spa permit requiring facility inspection and technicians licensed (typically by the state) to provide services
- Pool permit requiring inspection and regular water quality testing
May require lifeguard and or CPR certification as well as handicap accessibility equipment.
- Septic system inspection and approval by local or state health department.
Septic capacity whether private or public may limit the number of guest accommodations, dining seats and may limit future growth.
- Parking may not require a permit for on site parking but the local authority may require you to have a stated number of onsite parking spaces to accommodate guests, staff and owners, if in residence. This may limit future expansion if space is not available.