THINKING ABOUT INVESTING IN COMMERCIAL PROPERTY? READ THIS FIRST.

Alan Rawlins - Kaleidoscope Property

A NUMBER OF INVESTORS ARE CONSIDERING ADDING COMMERCIAL PROPERTY TO THEIR PORTFOLIO.

Here, Alan Rawlins of Kaleidoscope Property Consulting gives some action points to consider when thinking about a move into this area of the property market.

A couple of weeks ago I was asked to speak at a Landlord Investment Show event. My presentation covered useful information for investors who were contemplating a first step in to the commercial property market.

Some of the audience were quite experienced investors in the residential market – with significant HMO portfolios – and it was interesting to note that many of them had a "How hard can it be?" attitude towards the commercial property route. After all, they said; if you know the ins and outs of residential property then commercial can't be harder – can it?

COMMERCIAL PROPERTY CAN BE A MINEFIELD

Professional commercial property landlords have amassed incredible wealth through private property companies, Pension funds and other large investors; with an increasing portfolio of commercial assets under management over the past few years.

Likewise there are a large number of smaller investors who have quietly created long-term income streams from physically poor looking properties which produce great cash flow. It's these successes which have encouraged others to get on the commercial property bandwagon.

Conversely, there have also been some spectacular commercial property failures over the years mainly as the investor has not asked key questions before signing on the dotted line.

A WISE INVESTOR DOES THEIR HOMEWORK

If you regularly follow public auctions you'll have noticed a shift in the type of stock being offered for sale; especially by regionally-focused auctioneers. Lot sizes have increased; especially of mixed use assets, and the number of properties being put to auction has also risen.

The commercial asset will normally be seen as a cash generating business in its own right. However, these types of asset present their own challenges. When a property comprises maybe 10 or 20 different types of tenancies, each one poses its own potential issues which must be investigated before you make an informed decision on how much you are willing to pay for the asset.

Only a couple of years ago some of these larger lots now at auction would have been offered to a targeted list of pre-selected buyers and a successful sale would have been concluded following this so-called 'open' market exercise.

These days, vendors of property with an angle to exploit - such as redevelopment, conversion or mixed use potential - have shifted many of these sales to a more public option in the belief that they will secure a better price. This is where the inexperienced residential investor comes in. They will have reviewed the sale particulars and identified a 'resi conversion' angle for the property. They may then acquire the asset without fully understanding what they are buying, or knowing whether what they want to do 'subject to planning' is practical or even possible.

I offer these five points to help you with your commercial property acquisition plans, and to try and prevent you from making costly errors.

1. IS THE PROPERTY VACANT?

Don't assume that the property is vacant, even if the particulars stress that it is. Instead, make sure you ask the following questions:

- What happened to the previous tenant?
- Was the last tenancy subject to a lease?
- If so, has that lease expired, or was it bought to an end through forfeiture or surrender?
- Did the tenant go in to administration?
- Has the landlord placed the property in administration?

Do make sure that your advisors look in to the details here as even if the tenant has vacated the premises it may still be subject to a lease. If it is still subject to a lease this can be exceedingly difficult and time-consuming to resolve, and will probably cause delays in the acquisition process. However, if you're aware of any issues before you begin the process you can make allowances and plan accordingly.

Lastly, if the property you want is in an auction or being offered directly by an agent at a low purchase price you should ask why this is the case. If it looks like a very good deal, be aware of potential downsides. If it looks too good to be true it probably is.

2. TENANCY DETAILS

So, the property has got a tenant and you are going to get rental income from day one. But what sort of tenancy is it?

- Protected
- Excluded
- Licence
- Tenancy at Will
- Periodic

At this stage it's important to get the tenancy document, tenant's details and anything else relating to the tenant's right to be in the premises.

If you are relying on receiving rental income after your purchase, try to make sure the tenant can afford to pay the rent and intends to carry on doing so. Don't assume that historic trading data gives a

current picture of the tenant's financial health as this data could be two years (or more) out of date by the time you purchase the property.

There are three more questions you should ask at this stage:

- Does any agreement for lease contradict the actual lease granted on the property?
- Are there any existing Housing Act or Rent Act tenancies? The upper parts of older high street retail premises may have not been refurbed for a considerable period of time and could still be subject to a protected tenancy
- Are there any easements over the property or any other historic rights of way?

3. GET YOUR LEASE CHECKED BY AN EXPERT

Don't assume that the selling agent has read the lease or understands the impact it may have on the value of the premises or rental income you could achieve.

Make sure you get the signed copy of the lease (with appendices and schedules) and not the unsigned version or earlier drafts as these can be different. Always ask a commercial conveyancer to review the lease. This could end up saving you many thousands of pounds on the transaction in the long term.

Your commercial conveyancer will carry out the usual searches as well as making sure that the provisions of the lease don't breach local planning by-laws or other restrictions that might be on the property.

4. ARE MEASUREMENTS ACCURATE?

Please check the area and dimensions of the property yourself and don't assume that measurements in particulars or brochures (even glossy ones!) are correct. It's likely that the measurements have come from the seller's records and may have not been verified by the selling agent. Relying on historic data can be costly if inaccurate information is included in contracts and not checked until it's too late. You should also check if the right measurement approach has been taken as different types of building are measured in different ways.

5. VALUE

Now you have all the relevant information you need, does this affect the value you have placed on the property?

There are different methods to follow when arriving at a value which depend upon the type of property being assessed. Should it be 'Zoned', 'Overall', 'Gross' or 'Net'? Have any adjustments been made for physical attributes? Have any other factors been found in the lease which will affect the assessment of value for the property?

Valuation is not an exact science but relies on the valuer's opinion, based on their experience, and evidence from comparable properties.

If you follow my five points, know what to look for and what to ask, there are still some good opportunities to be had for the well-informed investor to exploit.

Contact me now on 020 3727 5024 for advice on how you can get your commercial property project off to the best start.

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