

Commercial Property Investment Guide

Your guide to purchasing and managing
a commercial investment property



first national
COMMERCIAL

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Introduction

Property represents a very secure and sound, long term form of wealth creation. As such, Australians are increasingly turning to property investment to secure their future.

A well managed investment can offer many advantages, including income and capital growth. Many investors may also be able to use their investment to reduce tax payable on their assessable income.

Commercial property is also a good option as part of an investment portfolio, particularly with people who do not need immediate access to their money and wish to protect themselves against inflation over the long term.

It is important to be aware however, of the responsibilities of managing your property investment and assuring proper care and responsibility.

As considerable money is at stake, you need to take the time to get good advice before you act.

This booklet is the first step in this process and is designed to provide an overview of the considerations required for any owner of a commercial investment property.

Remember, consideration of any investment presents wide and varied alternatives and there are always plenty of experts ready to pass their opinion. It is wise, therefore, to always seek appropriate advice from a qualified financial advisor or your accountant.



The benefits of commercial property investment

A well chosen commercial property should provide a good steady return on investment and, over time, increase in both rental potential and property value.

Good tenants or lessees will assist in increasing equity in your property and if well maintained will always be a tangible asset.

With the assistance of a good real estate agent providing the best in service, the managing of the investment from the landlord's point of view is relatively easy with little time required.

Why invest in property?

There are some good reasons to invest in commercial property including:

- Property is a solid, long-term investment
- Property investment provides capital growth
- It's an investment which is not too difficult to follow
- Property market information is easily accessible and widely available
- It is tangible – you can actually see and drive past your investment.

Financing

There are a number of different options available for financing your investment property through a range of lending institutions.

One of the most common forms of financing is that secured by mortgage. Mortgage repayments can have fixed or variable interest. There are options also to use a revolving credit facility to draw on the money.

Financial institutions such as banks, credit unions, etc. will have details on the different options available to meet your specific needs.

First National Commercial can offer you its own loans service with specific property investment rates. Finance can be arranged from a range of lending institutions to ensure the best possible deal for you. Details can be obtained by contacting your local First National Commercial agency.

Using home equity

If you do not have or prefer not to use cash for a deposit, you can borrow against the equity in your own home.

A home equity loan may be used to cover such aspects as the deposit, associated costs of purchasing such as stamp duty, legal fees, etc and perhaps commitments during any vacancy periods.

Negative gearing

Negative gearing is a common term associated with property investment. In simple terms, it refers to the situation where your outgoings may, particularly in the early stages, exceed the incoming rent of the property.

Where this occurs, there is the ability to gain tax advantages through claiming tax deductions on the outgoings.

If you are a PAYG taxpayer, you don't necessarily have to wait for the tax adjustments. You can apply under section 221D of the Income Tax Assessment Act for a tax reduction.

Nonetheless, negative gearing is not for everyone because there are some risks. Property values may decline from time to time, the flow of rental income may be interrupted, interest rates may rise or your ability to finance the cost of your borrowings may suffer. Investors need to take account of their ability or willingness to deal with these risks and to discuss them with their advisors before negatively gearing an investment property.

For further advice on negative gearing and appropriate application to Australian Tax Office, we would recommend consulting your accountant or financial advisor.

Successful investment in property looks to increasing income and property value in the long term. Investment in property is not suitable for the short term, even though it sometimes can provide a benefit.

Insurance

Specific insurance packages are available to property investors that not only cover the normal building and contents but also protect you against rent default up to a specific period, vandalism by tenants, etc.

Your real estate agent or insurance company can provide further advice on such aspects.

Choosing an investment property

Just because you may be a first time investor doesn't mean you can't choose to invest in commercial or industrial property. The principals are similar to any property investments and the results can be even more rewarding.

We all expect our investment property to grow in value, both in the eventual capital value and in the rent that it will generate. Therefore a choice needs to be made on two important criteria, location and quality.

Keep in mind that this is not a property that you will occupy and always look at the property through the eyes of a potential tenant.

A property located close to transport, with good access and parking facilities will be in greater demand and usually command a higher rental.

The building, too, needs to be desirable and a size to suit the area's potential.

The building should be sound and as low maintenance as possible. As a rule, more modern buildings require less upkeep and are usually more desirable to tenants.

All First National Commercial agents offer and are experienced in Investment Property. You'll find them happy to assist you through the purchasing process.



Who manages the property?

All property requires ongoing maintenance!

There are landlords who take an active and hands-on role in the management of their property and those who are happy to have an agent professionally manage their investment.

Obviously those who manage their own property must be prepared to oversee their own repairs or organize a qualified tradesman, do their own cleaning and collection of rent. Preparation of leases are usually done by a solicitor.

Frequent changes to Acts of Parliament in each State mean changes to the way the property is administered. Many of these include administrative duties like appropriate records being kept, for example receipting, access notices for inspections, inspection sheets, bond investments or bank guarantees.

In addition, they are required to:

- ▶ Ensure the premises are clean/secure and fit for occupation at the beginning of the lease
- ▶ Ensure all facilities are in good working order and safe
- ▶ Be available to arrange urgent or essential repairs

It is vital that all landlords who manage their own property are completely familiar with the legislation in their state which governs industrial or commercial tenancies.

What costs will I have to meet?

As you'd expect, there are various costs associated with property investment in addition to the maintenance costs.

When you acquire a property, there are government charges by way of stamp duty and registration fees on the transfer of title and mortgage. There are also solicitors' fees.

In addition there are real estate agents' fees for managing your property and selling it if you decide to do so in due course. Your real estate agent can assist you in the calculation of these costs.

How much do I rent the property for?

As with any rental property, your commercial property must be able to meet the market and be competitive with other properties being leased.

If managing your own property, it is essential that you compare your property with that of others by using comparative market analysis, in which all aspects of the building and its location with several others of similar size and type.

This may be difficult to do given that you may not know the rent charged nor the condition of the property and internal improvements.

An experienced property manager can provide a market analysis. He or she can inspect your property and compare with similar commercial or industrial properties under their management.

Because they are aware of the rental market they will be able to set a rent which will allow your property to be rented at the earliest possible opportunity, whilst ensuring you get the best return for your investment.

Marketing your property

Marketing your property for leasing is something that needs consideration.

Highlighting your property amongst the myriad of other properties being advertised is a difficult task.

The rent being asked, location and attributes of the property area are all aspects that prospective tenants will take into account when considering a property to be leased.

A real estate office regularly attracts many rental inquiries from prospective tenants waiting for properties.

In addition, their expertise in marketing and presenting advertisements in many cases can make the process far more effective than a landlord could achieve themselves.

Your property on show

Prior to renting your property, you should look at any improvements or maintenance that should take place.

The better your property is presented, the easier it will be to rent and you are more likely to attract better quality tenants.

Particular attention should be given to:

- Well presented and tidy property and surrounds including any gardens,
- Minor repairs,
- Cleanliness,
- Having carpets professionally cleaned in office and any necessary re-painting,
- Clearly marked car spaces.



The tenant

The next step is to lease the property.

Selecting a suitable tenant for your property is extremely important.

As such, you need to select someone who you believe will look after your investment and be in a position to pay the rent.

Remember, you will use money from rent to offset your investment loan.

Privacy legislation may prevent you from gaining credit checks, however real estate agents have processes in place that assist in tenant selection, including reference checks through agencies established for this purpose and gaining thorough business and management details.

They may have a list of prospective tenants waiting for particular types of properties.

Other duties that a landlord may have to perform:

These additional duties and responsibilities are required of a landlord or a real estate agent.

- Arrange repairs and maintenance
- Strict arrears control
- Arrange inspections of properties for prospective tenants
- Legislation may require the provision of a trust account for the safe keeping of the rental bond or lodgement of the bond with an independent authority such as a rental bond board.
- Prepare detailed condition/inspection report
- Arrange insurance, rates and other payments
- Prepare applications and arrange for the serving of notices in compliance with relative legislation or tenancy agreements

Insurance

It is vital that your property is well insured ie; the building, any fittings or fixtures, public/legal liability.

In addition, there are insurances available for malicious damage and loss of rent through default which will give you the owner, great peace of mind. These are a necessary safeguard for a rental property.

CHECK YOUR INSURANCE COVER!

Landlord protection insurances are available through real estate agents.

What does a property manager do for you?

Most real estate agents will have a property management department which is solely established for managing investment properties.

The level of service will vary and depends on the structure of the office, the real estate company's approach to property management and customer service.

In the main though, your real estate property management services will include:

- Negotiation of an appropriate lease
- Organise the advertising for the property for rent
- Showing prospective tenants through the property
- Receipt of applications and screening of appropriate tenants
- Optional checking with Landlord on screening new tenants
- Completion of relevant documents
- Instructions to prepare leases to solicitors
- Receipt of rent monies
- Follow up on any arrears in rental payments
- Organisation of repairs/maintenance
- Provide the landlord with regular payments and statements
- Payment of accounts
- Conduct initial, final and routine inspections of property
- Bond collection or bank guarantees and the first month's rent in advance prior to tenant moving into the property
- Investment of Bond in accordance with the lease
- Provide Insurance
- Personal service from trained and local property management team

Legislation

Each state has legislation governing commercial tenancies and it is vital that whoever is managing the property fully understands the requirements and the obligations of landlords and tenants.

How to select an appropriate real estate agent to manage your property

Making sure you have the right real estate company managing your investment is vitally important.

A good real estate company saves you time and takes the hassle out of owning your own investment property.

Here is a checklist of some areas you should consider when selecting a real estate company to manage your property.

- Does the company have property managers solely designated to the task?
- How will they communicate with you and how often?
- Do they have a good knowledge of the local commercial and industrial rental market?
- How many properties do they manage?
- Do they have property management systems in place?
- What is the property manager's knowledge of the appropriate legislation?
- Do the property management staff attend regular training?
- Do they have the support of a larger network?
- What is their approach to selecting tenants?
- Do they have systems for following up arrears?
- What systems do they have for collecting rent and reporting to the landlord?
- Can they arrange insurance and payments of all outgoings?
- How effective is their website and online marketing?

Budget for commercial property investment

This form will help you estimate your income against your expenditure on your investment property.

Income

Rental Income per annum: \$ _____

Expenditure

Advertising \$ _____

Agency Fees \$ _____

Letting Fees \$ _____

Maintenance / repairs \$ _____

Loan Repayments \$ _____

Insurance \$ _____

Rates and Taxes \$ _____

Depreciation (if applicable) \$ _____

Body Corporate fees (if applicable) \$ _____

Other \$ _____

Balance \$ _____

In many cases, commercial, industrial and retail leases are net leases. Net leases allow the investor to pass on most property costs to the tenant. This form of lease protects the investor from increasing costs during the term of the lease thus ensuring the yield on the investment is secure.

Your First National Commercial agent would be happy to explain the difference between both net and gross leases.

Agreements between landlords and tenants

A lease/tenancy agreement will be prepared which specifies the rights and obligations of the landlord, agent and tenant.

This is a legally binding document enforceable under the relevant State legislation.

The legislation is designed to protect the consumer. It is open to interpretation and change and therefore it is vitally important to have a good working knowledge of the Act.

Leases can be of varying lengths but generally are for one year to 5 years or longer.

The lease has standard and special conditions as required, and will include the following:

- Rental payments
- Length of the lease
- Requirements of the landlord, clearly stated with expectations and obligations of the tenant
- Notice of vacation that must be given either by the landlord or tenant
- Security bonds or bank guarantees
- Special conditions as presented by the landlord/agent and agreed to by the tenant
- Rent reviews

Agreements between landlords and real estate agents

A landlord will be required to complete a management agreement which engages the agent to manage the property on their behalf.

The agreement documents all aspects of management and outlines performance and responsibility by the agent.

Agreements may be altered or updated as circumstances change.

Included in the agreement will be:

- Agency fees
- Regularity and reporting inspections
- Details of payment to landlord
- Level of expenditure and process in relation to maintenance / repairs
- Notice required for cancellation of agreement

Your guarantee of service

As First National Commercial is the first network to introduce an internationally accredited quality assurance of service for its property management operations, our progressive agents practise this ISO 9001 ensuring their genuine commitment to meeting the client's needs.

What your First National Commercial property manager can do for you

First National Commercial offices offer a complete commercial property management service for property investors.

Being part of Australia's largest and most successful real estate network of over 450 offices, the marketing services, web systems and professional development are at the leading edge of the industry.

First National Commercial Property Managers are well known for attention to detail.

For the care of your valuable asset, First National Commercial Property Managers prepare a written inspection report at the commencement of each tenancy and ensure a rental bond is lodged.

An inspection of the property when a tenant vacates is a standard procedure within First National Commercial and bonds will only be released if the condition is satisfactory.

Inspections are conducted during the tenancy and important repairs and maintenance will be arranged, with your approval.

Financial transactions are conducted with efficiency and receipts are issued for all monies received on your behalf. You are accounted to regularly and monies are paid by cheque or deposited to an institution of your choice.

We can arrange insurance which not only covers your property, contents and public liability but also the possibility of loss of rent.

Your First National Commercial Property Manager has local expertise and establishes the rental value by comparing your property and similar properties currently let.

By maintaining your asset in good repair and ensuring it is well presented you will maximise rent, reduce vacancy and attract a high standard of tenant.

Vacant properties cost you money and are a security risk.

First National Commercial offers expertise in commercial property investment and can assist in building your portfolio as a secure means of investment for your future.

First National Commercial Property Management Services cover Residential, Commercial and Industrial property.

We can help you with Essential Services compliance, tax depreciation schedules that greatly improve the overall performance of your asset and many of our members offer competitive finance broking services.

With over 450 offices in Australia, New Zealand and Vanuatu together with associated links with overseas networks including Prudential Referral Services International, we can offer services anywhere and attract tenants from far and wide.

As mentioned earlier, First National Commercial offers a quality assurance of service unique in the industry.



Terms relating to property investment and management

Lease/tenancy agreement is an agreement for possession, not ownership, of a property for a set period.

Lessee/tenant is one who leases/rents a property from a lessor/owner.

Tenancy Agreement document sets out details of the property to be rented and the terms and conditions agreed to between landlord and the tenant.

Landlord/lessor is the owner of property being rented.

Negative Gearing is where the costs associated with your property investment exceed the income received over the tax year. This loss can be used to offset other income in that year's tax return.

Net Yield is the income on your property less certain expenses such as rates, insurance, maintenance and body corporate levies.

Depreciation is a non cash allowance that you may be able to claim on your tax which reflects the limited life of an asset

Capital Gains Tax is the tax based on the difference between the purchase and selling price, less inflation, applied upon the sale of an investment property.







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1800 032 032
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