Management rights

Enjoying a resort lifestyle while looking after other people's properties could be rewarding for the right type of investor. LAUREN CROSS

It's often described as a home with an income, considered a dream way to make sure your investment is being well looked after. Management rights can allow you to live in places you might not otherwise be able to afford, or make money out of properties that aren't yours. In fact, a large management business can make more than $1 million per year, according to Hynes Lawyers partner Frank Higginson. But finding the right type of rental accommodation or unit complex can be tricky, so before you get ready to sip on a pina colada while enjoying ocean views from your balcony, it's important to know what's involved when you buy management rights.

WHAT ARE MANAGEMENT RIGHTS?

Australian Management Rights (AMR) says management rights allow you to take care of a property or complex on behalf of the body corporate (owners corporation). In most cases you can live on the complex and you're usually in charge of either permanent or holiday rentals.

"A combination of investment return, a combined home and business environment and the lifestyle aspect has proven to be a very attractive business proposition," AMR says.

"In other instances, management rights have been chosen by people seeking a home with some part-time work; a home that will enable a retiree to keep active, or a home that will allow a single parent to be at home with the kids. Management rights are often seen as buying a home which allows for a better lifestyle."

This, of course, sounds like a pretty good deal. However, there are also big responsibilities involved, with four main components of the business. They are:

1. A manager's unit – Usually located in the most central position in the complex, to allow the manager to service the needs of residents and guests. The manager's unit can also involve the exclusive right to occupy another part of the common property, such as an office or reception area. Alternatively, this area will be included as part of the title to the manager's unit when you sign up to buy your management rights.

2. A management agreement – The body corporate appoints the manager as the caretaker of the complex. The agreement states that the manager is responsible for carrying out certain duties within the complex, and the manager is paid remuneration, usually in accordance with increases in the consumer price index.

3. A letting agreement – The body corporate appoints the manager as the letting agent for those who are renting their unit out. The owners are still able to let their units through an outside real estate agent if they prefer, but it's often more convenient and beneficial to go through the onsite manager.

4. The by-laws – These are rules that govern the operation of the complex and set guidelines for community living. They usually contain very important provisions that protect the manager's exclusivity within the complex as the only person who can operate a management and letting business.

Higginson says management rights can be applied to all kinds of property developments, from the traditional unit, townhouse, villa or resort-style development, right through to corporate letting, student accommodation and even small retirement villages.

ISTOCKPHOTO

"One of the most important aspects of the agreement is whether it's personal or supervisory in nature," Higginson says.

"Personal agreements are ones that require you to perform the work personally, or through contractors or employees paid by you. Supervisory agreements are ones where the duties are performed by contractors or employees who are paid by the body corporate, but supervised by you."

Director of Property Pacific Real Estate Jan Grover says when you purchase management rights, to become what's known as the resident manager, you're employed to be the body corporate's custodian.

"Managers are also usually paid from $1000 to $1200 per unit per year to look after the complex, although it does depend on the size and location," she says.

"You're also assigned the letting rights for the complex, which means you're in charge of letting individual units."

Generally the more units you rent out, the more money you receive. Grover says the figure is usually between 7.5 per cent and 8.2 per cent of the rent, or in the case of holiday and periodic letting, as much as 12 per cent. However, don't be fooled by the dollar signs – more money also means more work.

"From a manager's point of view, in a permanent letting situation you can structure your working hours, so you're less likely to have interruptions in the middle of the night," Grover says.

"If you're managing a holiday unit you might have people arrive late by plane, or you may be called to remind holidaymakers that their fun is also noisy for their neighbours."

TRAINING REQUIRED

Principal of Kapitol Brokers Monty Van Dyk says investors hoping to rule their investment roost must obtain the required training.

"There's a fundamental requirement under law, which requires a manager to be the holder of a restricted letting license," Van Dyk says.

"It's different state by state, but all of them require a minimum qualification, which is a certificate through a real estate body. Most institutes have a course of some sort too."

Higginson says the New South Wales industry is based on the Queensland model.

"In New South Wales, a residential unit manager must obtain an onsite residential property manager licence rather than a restricted letting agent's licence," he says.

"One of the most important differences is that all new management rights agreements are limited to a term of 10 years."

Van Dyk says the Australian Residential Accommodation Manager's Association is an industry lobby group, which is currently trying to get NSW more in line with the Queensland legislation.

"What we're looking to achieve is national regulation of the industry, so everyone is on the same playing field," he says.

Chief executive officer of Elite Manager Training Rachel Irvine says colleges have also recently added onsite management to their list of courses available.

"The sole purpose is to upskill managers," Irvine says.

"These courses and certificates help refine managers in all areas of body corporate relationships, with office operations, marketing, and health and safety included. There's a pre-purchase certificate course, and there's also another one where existing managers can improve the skills they have."

A large management business can make more than $1 million per year, according to Hynes Lawyers partner Frank Higginson.

Irvine adds the biggest problem is managers who love property, but don't know how to run the business of it.

"If the manager is making money, the owner is making money and everyone is happy," Irvine says.

"If the managers aren't making money, neither are the owners. We want to reduce that risk by getting better managers and upskilling them before they buy. We don't want them to figure out 18 months into it how to improve the property – we need them up and running in the first week of buying the business."

DO YOUR SUMS

Grover says it's important investors think carefully about the type of management rights that suit their business and family objectives.

"A lot of people say it's a lifestyle business. Yes it is, but you also have to mow the lawns, clean the swimming pools and toilets. If you're in a position where you can buy a large complex, you obviously have a larger remuneration coming, so you can employ people to do the work for you, but with a smaller business you'll carry the load yourself," Grover says.

Investors should also make sure they do their sums, as most management rights range from $300,000 through to several million dollars.

"From a business perspective it's prudent to assess how much of the purchase price is spent on the unit," Grover says.

"You might have a lovely unit on the beach which therefore has a high real estate value, but you end up spending all your money on the unit, not the business. If you want a good return on your money, too much money spent on the residence won't help."

Grover adds managers should expect to pay slightly more for their unit than others in the building, usually by about five per cent. This means if other units are valued at $300,000, you should expect to pay $315,000.

"Then you have your business price, which is determined by the revenue generated. It could be anything from 3.5 to 5.5 times the net profit (the revenue minus expenses), depending on the complex.

"These businesses can be a little bit more expensive than something like a restaurant, because it's proven revenue with no bad debts."

Higginson says verifying figures and other transaction documents in the purchase process is critical, so when the management rights business is later sold, there's a clear understanding of what's actually being sold.

"Vendor-prepared figures don't necessarily take into account the latest industry trends in terms of verification issues, and purchaser's accountants usually tear them apart – sometimes just for sport."

He says horror stories exist both ways.

"We had a client last year purchasing a complex off some vendor-prepared figures. The vendor had made a mistake in their calculations and understated their income by $20,000. Suffice to say, we were instructed not to slow anything down in the matter and this created a windfall gain for our client on settlement."

Higginson says investors also need to know what fees they can charge.

"In recent times we've had several instances where vendors have been charging amounts different to those recorded in their appointments, for example, a postage fee of $4 per month in the appointment, but the invoice was $7 per month. While this

Legal and tax implications

MBA Lawyers partner Clayton Glenister says there are usually capital gains tax (CGT) implications with management rights.

"Depending on the structure, your unit may be a principal place of residence, so there won't be CGT there," Glenister says.

"However, usually there will be CGT on the business, like any normal business structure. The more the business makes, the more tax you pay. There might also be rollover relief if you put funds back into another business."

Hynes Lawyers partner Frank Higginson adds the way you set up the business structure could help reduce the tax you pay.

"Buying a business in some form of corporate entity as opposed to your personal name can have significant tax advantages," he says.

"Using an incorrect entity to purchase can have significant tax and asset protection consequences at a later stage."

Glenister says it's imperative buyers check the fine print and profit of the business before signing any agreements. He believes anything with less than 20 units won't be suited to having an onsite caretaker and letting agent. This is because most managers earn $1200 per unit per year, along with rental income. You also pay about $1800 on license fees.

"Those with net profits of $80,000 or less, there's just no demand for them because you can't have mum and dad running the business together. You would have to get another job to support the income," he says.

On the other hand, Glenister has also seen cases where managers make more than $800,000 per year, usually in larger complexes. He says investors should probably opt to go through one of the 'big four' banks for loans, because they often have brokers who specialise in management rights.

"Any buyer needs to make sure they have both an accountant and a lawyer who specialises in management rights. As part of the contract they buy, they have to verify the income the business has derived in the last 12 months, which is all done on what's called 'a multiplier'."

The higher the multiplier, the higher the annual profit. For example, a large high-rise holiday-let building would have a multiplier between 5.4 and six times the annual net profit.

"If the building has a net profit of $300,000 and the multiplier is 5.5, it means the purchase price is around $1.65 million.

"Some agreements are trading for up to $13 million but the strength of your buying is the legality of the caretaking and letting agreement. Only a specialised lawyer can determine this for you. If the agreement isn't lawful you run the risk of the body corporate terminating your agreement, which therefore could leave you with nothing to sell."

You may also need insurance in case you get sick, or if someone has an accident and tries to sue you. Higginson says managers should make sure they have professional indemnity and public liability insurance.

"If someone trips and falls, a body corporate might say you're to blame because you were negligent. This is where professional insurance is needed," he says.

In the worst-case scenario, a body corporate might try to terminate your caretaking role, but you would still own your unit and letting rights.

"If you end up in court usually it's over bond disputes and rental arrears acting as an agent for owners to chase defaulting tenants," Higginson says.

Glenister adds a manager should also check the hours of work aren't "ridiculous".

"You need to look at your protection and make sure there's exclusivity for you, so your lot is the only unit that can be a manager's unit. Also make sure you're not going to become a servant. Sometimes the office hours are 7am to 7pm. They expect you to keep the office open during that time, plus open Saturday and Sunday and also do all the cleaning. There needs to be a life and work balance."

Even worse than working hard is working out problems. Glenister warns it's important to get an industry expert to go through all the books of the body corporate meetings and the accounts before the purchase.

"The last thing you want to buy is a headache. Get your lawyer to go through the records, look at the minutes and see where the issues are," Glenister says.

might seem a small amount, it becomes a lot larger when you multiply it by 12 months and then across 100 units in a rental pool, and then by the multiplier on the sale.

"If you get to the stage where more than 20 per cent of your appointments don't comply with legislation, or aren't assignable, there's going to be trouble with your sale."

THE PROS

You may still be wondering why you should buy management rights, rather than just a unit in a complex. Grover says the main advantage is that management rights are a safe investment.

"It's favoured by the banks from a lending perspective because the income is transparent," Grover says.

AMR says there are heaps of other benefits too. There are no bad debts, because you're paid your remuneration by the body corporate each month, and you also receive money from the units you let out.

"You only need money to survive until the end of each month," AMR says.

"Many of these complexes, particularly in permanent let complexes, can offer a unique lifestyle. By lifestyle we mean the ability to enjoy the facilities your own complex might offer."

Unlike restaurants and shops, there's no wastage either.

"There's no stock sitting on the shelf eating its life away. These businesses are people businesses, where you're in a unique position of having a combined home and business. You can also live onsite."

Finally, AMR says they offer security.

"Provided you keep the support of 51 per cent of owners who vote at meetings, there's every reason to believe you can have your agreement extended and remain as the resident unit manager."

THE CONS

While every unit owner is your client, AMR says they're also your boss.

"If you aren't comfortable with this concept, don't buy management rights," AMR says.

"You're also answerable to the committee members. In addition, you have to deal with tradespeople and the many others that flow through the complex."

Another downside is that although management rights are often referred to as a 'lifestyle choice', the opposite can actually be the case.

"Most people, when they have a bad day, simply retreat to their home and their problems are soon forgotten. In a management rights complex, the problems are still all around you as your home is your business. In the case of a high-rise complex, the problems are also above you. You have to be able to live with this fact."

Higginson says a source of some contention in larger complexes is usually the number of staff required to operate the building or site.

"The standard management rights contract says the net profit will be verified, based on what work a two-person management team could perform," he says. "Where there are additional staffing requirements beyond that two-person team, it's sometimes a question of balance as to what is actually required to run the business, as against what is a lifestyle choice for that particular vendor."

Van Dyk adds management rights buyers only require a relatively small deposit for management rights – usually the banks will lend up to 70 per cent.

"The generous lending on a management rights business is a reflection of the stability and security of the industry," he says.

WHO IS SUITED?

An investor who goes down the management rights path must be a "people person", according to Grover.

Grover suggests "practical people" will probably do better as well. This means people who are good problem solvers and able to build strong relationships with property owners and their tenants.

In lots of cases, a husband and wife become managers together.

"It's ideal for a couple, but lots of people are very good on their own too," Grover says.

"You might also find most management rights owners are mature people, simply because they've amassed the money.

"Sometimes young married couples buy a smaller business that the wife can run on her own. It's seen as buying an investment with an income."

Van Dyk adds from time to time, managers buy an investment but they're unsuitable for the industry. He says it's important for a body corporate to approve the right incoming manager, and for a manager to have a business-orientated mind.

MBA Lawyers partner Clayton Glenister adds that having a letting manager living onsite at the body corporate complex is advantageous for investors.

He says, "If my tenant or holiday guest has a problem with the apartment, such as a broken tap, the onsite manager will be able to deal with it then and there, even at 2am. If my unit isn't with the onsite letting agent to manage, it might take a number

A typical example of a management rights high-rise in Brisbane

PROPERTY PACIFIC REAL ESTATE

of days for my property manager to organise the contractor to get there."

For this reason, Glenister believes laws should be introduced to only allow onsite letting agents the right to holiday let.

"Having someone at ground zero means the guest is more inclined to enjoy their stay and the apartment is better looked after, which means better returns," he explains. api

CASE STUDY

Investing in investments of others

Name	Zac Marshall
Lives	Caringbah, NSW
Invests	Sydney, NSW

Since becoming involved with management rights, 28-year-old Zac Marshall has learnt what not to buy.

Ironically, the young unit manager now only invests in houses.

"I see all the problems you have in a unit complex, you don't have control over everything," he says.

Zac started his own management rights company, Result Property Group, last year. He doesn't live onsite but manages around 25 complexes, earning from $2000 to $100,000 for each complex. He also charges the body corporate (also known as owners corporation) a fee for attending meetings after hours. Zac's job not only gives him cash to buy more properties, but also allows him to learn more about the property market and make better investment decisions.

Despite taking care of some very big buildings, he believes the smaller complexes are the hardest work.

"I have a building of 100 units and they're all fine. But I have another building of 12 units and they're fighting all the time, saying 'I don't want this done', or 'I don't want this colour'. Pretty much you're the mediator, so you have to make sure everything is above board and done to a vote."

A common problem he faces is owners who want to keep pets, even though it's against the by-laws of the complex. Others renovate their kitchen or bathroom and expect the body corporate to pay.

"They try and fight you over it, and when you've got people screaming at you it can be very stressful, so you have to have thick skin."

A typical day involves taking care of the administration side of things, paying bills, sending levy notices and taking care of the common property. You're also on call 24-seven.

"People say you're not always on call, but those people aren't doing their job properly. I had a fire in one of my buildings and they called me at 3.30am. You have to listen to what your clients say, so in a way your clients are your boss."