COMMERCIAL REAL ESTATE

Sale-lease-backs still a viable option?

When a business experiences a transition of leadership, a sale and then a lease-back of the property might ensue.

Our practice centers on family-owned and operated manufacturing and logistics businesses experiencing a transition.

Recently, I wrote about common transitions a small business experiences, such as the dissolution of a partnership, sale of a business, acquiring a competitor or the unfortunate circumstances of the death of a principal, divorce or some other distress within the enterprise.

As reviewed, all of these transitions come with their own brand of commercial real estate solutions.

As an example, when a competing company is acquired, two cultures must be forged into one — akin to a blended household. As you can appreciate, this can cause some drama. As the operations are morphed, so must the locations from which they occur. Frequently, redundancy is experienced.

Specifically, two buildings within the same submarket where only one is needed means, consequently, one must be jettisoned.

But let's examine the flip side: the seller of the acquired competitor.

When the sale of a business happens, the addresses from which the trades are plied are either owned by the principal selling or leased by said principal. In the circumstance mentioned above where two facilities are within the same geography, two different strategies are employed.

If the redundancy is leased and a decision is made to abandon the building, we can sublease, pay double rent until the term boils off, or default, which is never recommended. If owned — without an occupant — we can sell the empty building or lease it and hold on or possibly sell the leased location to an investor.

But how about the chosen building — the one selected to carry forth the business of the company and not deemed excess? Then what? A building owner finds herself in a position to assign the lease agreement if appropriate, or sell or lease the building to the acquiring group.

All of the above scenarios contemplate the moves made AFTER the business sale. But are there maneuvers before such a liquidation? Certainly.

And I'll spend the balance of my words describing one such arrangement — the sale-lease-back. If you're unfamiliar, a sale-leaseback allows the owner of the location to liquidate the real estate while allowing the occupying company to remain in residence under a long-term lease arrangement.

We were fortunate last year to complete five sale-lease-backs. Four of the five were done in anticipation of a sale of the occupying companies. In one case, a principal's death caused disruption and the need to quickly restructure and liquidate for the heirs, who had no desire to own a company or the real estate it occupied.

In the other three, the principal had experienced a business downturn from the pandemic but wanted to capture the appreciation of the real estate today in anticipation of a business sale in a couple of years.

So why do this prior to a company's sale? After all, rent no longer will be received by the seller. In our experience, the reasons that follow are typical.

A market rent is established from which a company's value is derived.

Real estate values ebb and flow. Taking advantage of a hot market can make sense.

A marketable lease can be structured — with appropriate lease rates, terms, increases and maintenance responsibilities.

You may be wondering: Does selling real estate prior to a company sale affect the company buyer pool? It indeed can, and this should be carefully considered before such a strategy is completed.

How, you may wonder? As mentioned above, a buyer with similar locations may view a long-term lease as a liability. This occurs frequently when a strategic player emerges, such as a group in the same industry.

Allen Buchanan is a principal and commercial real estate broker at Lee & Associates, Orange. He can be reached at 714-564-7104 or abuchanan@lee-associates.com.