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### Deal Fatigue

Most of us have been involved in something that gets to a point where we are done and enough is enough. Buying or selling a business is often a very involved process and can certainly be stressful at times. Sometimes we see a buyer or a seller or both get to the point where they are done. This is called Deal Fatigue! We've seen it, we've helped many parties through it, and we've seen deals end because of it. While thinking about Deal Fatigue I am reminded of a past transaction that perhaps serves as a good example. Multiple challenges delayed the completion of the deal and nearly ended it all together. The first issue was that the sale of the business included the sale of the real estate. The real estate had been in the seller's family for a very long time. To be sure there were no environmental issues, an initial report/assessment was required and was completed. Both parties agreed to share the cost of the assessment. The results of the assessment indicated that due to the age of the property there was a need for some additional testing. This was not planned and ultimately delayed the process as well as caused the cost to go up. The question at hand was: Who pays the additional cost? The next issue was determining the price / value of the inventory, which was a major cost component. The seller had set a price, then evaluated and wanted a higher amount as he felt there was more inventory there than previously thought. Determining an actual higher amount would have involved bringing in an outside party to determine the value of the inventory and taken weeks. The buyer told us if that's the case, I'm done!

In this example, we were the advisor to the seller. On the inventory issue,

## Real Estate Transfer Issues

Part 1 of 2

The biggest obstacle created by ownership of commercial real estate in a business sale transaction is establishing the property's fair market value. (FMV). Commercial real estate values are much more difficult to determine than residential real estate values. As opposed to the housing market, where there are comparable and recent sales of homes to help establish value, that is not the case with commercial property.

Eliminate the obstacle created by unknown values of commercial real estate. Have your property appraised, not by real estate agents, but by professional licensed commercial real estate appraisers recommended by your broker.

### About commercial property valuation.

Commercial properties are usually fairly unique, with differing extents of construction types, build-outs of office space vs. warehouse space, size of land, types of usage, zoning ordinances to be dealt with, and the consideration of location, location, location. Since there are far fewer commercial transactions than home sales, actual sale comparables are hard to find. Asking prices are usually astronomical when compared to actual sale prices. So the few asking prices in the current marketplace are not reliable comparables.

### The business value is dependent on the real estate value

There is another complicating factor when a business owner also owns the facility the business occupies: the business value is dependent on the real estate value. Since business valuations are a function of the business's cash flow, the cost of occupancy at FMV has to be determined. In other words, if the owner owns the facility's real estate and the business is not paying the owner rent, the business shows no occupancy cost in its financial statements. In this example, in determining the cash flow of the business, the cost of occupancy would have to be considered and imputed (negative adjustment to cash flow). Before a business is valued, the cost of occupancy should always be adjusted to FMV. But when it comes to commercial real estate, it is not all that easy to do so.

### Benefits of obtaining a real estate appraisal.

There is a way to address this particular obstacle. It is imperative to obtain an appraisal from a professional and licensed commercial real estate appraiser. There are many benefits to doing so:

we intervened and explained what could happen if the seller took a hard line on the additional cost and time, and he agreed. As to the cost of the assessment and additional testing, we communicated to the buyer the value of having it completed. The result was that the additional cost was shared equally. At the closing, everyone appeared to be pleased, or maybe it was relief that the sale and purchase happened.

The sale of many small businesses is between a first-time seller and a first-time buyer. For us it might be transaction number 300 (we don't keep count). It's impossible to foresee all the potential issues in getting a deal done, but we do have a lot of experience. We do our best to explain the process to both seller and buyer to prepare them for what could happen. We do our best to anticipate what could be difficult issues so that we can offer alternatives and solutions. Deals do get done!

If you are buying or selling a business, don't do it without the guidance of professionals. Contact us to begin the process.

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- 1) By obtaining the FMV of the property's sale value and the FMV of leasing the facility, you can adjust the business occupancy cost appropriately and set a reasonable asking price for the business.
- 2) Buyers always have fear of overpaying. A real estate appraisal eliminates that issue, so you only have to reach an agreement on the price of the business.
- 3) Based on the information received, you can determine if you prefer to sell or lease the real estate to the buyer of the business.
- 4) If the real estate is to be sold, a lender will require an appraisal. When a recent appraisal already exists, and the lender's appraiser is made aware of the value, the second appraiser's value is likely to be similar to the first appraisal. Consider this: which appraiser is likely to provide a higher value, the one you hired or the lender's appraiser? Isn't it a good idea to have your appraisal ready for the lender's appraisal?

This concludes Part 1 of 2. Part 2 of 2 will be in our October 2022 issue. Don't miss it. If you feel our Newsletters are of value to you, perhaps you would share them with a Valued Business Partner?

## **NEXT ISSUE**

### **Part 2 of 2 - Real Estate Transfer Issues**

## **CONTACT US**



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