TOURISM PROPERTY

EXPLAINER

Management Letting Rights

How do Management Letting Rights work?

Owning a tourist accommodation property would normally require an investment of many millions of dollars. The Management Letting Rights (MLR) structure allows the small business operator to own their apartment and live onsite, plus operate the serviced apartment complex on behalf of the other owners.

The operator is paid a regular guaranteed Caretaking Fee to maintain the gardens and swimming pool plus, as the exclusive operator of the complex, can earn solid income from managing the apartments.

Quite often a Management Letting Rights property is a one person business, so one partner can keep their “real job”, this is particularly attractive with the new popularity of working from home.

MLR’s are extremely common in Queensland, but extremely rare in NSW outside of the Tweed Coast.

Are all Management Rights Schemes the same?

No. There are actually many different models for handling revenue and expenses. This will be set out in the Management Agreement.

Some schemes are “Residential” – meaning the Manager handles permanent rentals and Caretaking of the shared property. The schemes in the tourism industry are generally “Holiday”, where the Manager rents the apartments only as short term visitor accommodation, plus Caretaking duties.

How are Management Rights Schemes valued?

Firstly there’s Real Estate Value = the managers apartment, plus the office and any other spaces “on title” (perhaps storage areas, a café or even a function room). Then there’s Business Value = a multiple of profit. “Multiples” vary across states and markets, but can range from as low as 2.5 times up to 6 times profit dependent on many factors.

Example – XYZ Holiday Apartments	
3 bedroom Managers Apartment with double garage	$550,000
50 square metre office	$150,000
Real Estate Value	**$700,000**
Caretaker Salary	$45,000
Adjusted Nett Profit (Commissions + Fees – Expenses)	$95,000
Business Value (3.5 times multiple)	**$490,000**
Total asking price	**$1,190,000**

What do you advise potential buyers of Management Letting Rights?

Firstly, this could be an ideal business and home for the right people. Often it's a lifestyle choice – minimal working hours and a premium location to live in. It's a rare opportunity to live and work in the one place and use the business income to pay for your home ownership.

Here's a few basic tips:

1. Do your research, ask for help and professional advice.
2. Check the value of the managers apartment is correct in the local market.
3. Due diligence – check the profit & loss and income reports. Use an accountant if you need help.
4. Understand the Management Agreement and Caretaking Agreements, these set out the rules and requirements.
5. Consider the overall return on your investment, not just the Business Value multiplier – in our example $140,000 / $1,190,000 = 11.76%
6. Don't forget that a big part of your investment is Real Estate Value

Do I need particular skills?

Many Management Letting Rights owners are first timers to the accommodation industry.

You'll mainly need to enjoy dealing with members of the public as there are new people to meet every day. Most likely you'll have a small team of housekeepers to clean apartments, or this can be out-sourced to a cleaning company if you prefer.

Managing and paying external suppliers for laundry, apartment supplies and maintenance.
These days, much of the marketing is handled by Online Travel Agents such as Booking.com or Expedia - so most properties just have their own basic website.

You'll be handling funds for your apartment owners and will learn Trust Accounting with your real estate course – computerized systems make it very simple to manage.

Basic computer skills for guest accounts and to sell apartments online – much of this is automated.

Can owners get bank finance to buy Management Letting Rights?

Absolutely. In fact, banks will generally lend against the real estate (owners apartment, office etc) at residential lending terms and also lend against the business at commercial lending terms.

Banks might lend 80% against the Real Estate Value for a 30 year term and 50% against the Business Value for 10 years.

Example – XYZ Holiday Apartments, total value $1,190,000

Real Estate Value $700,000 @ 80% LVR = $560,000 residential loan, 30 year term
Business Value $490,000 @ 50% LVR = $245,000 commercial loan, 10 year term

Total loan of $805,000 or a 67.6% blended Loan-to-Value Ratio (LVR)

In this example, the Manager is making a profit of $140,000 per annum. From this, they could readily make Principal and Interest repayments.

Example – XYZ Holiday Apartments, total loan of $805,000

Residential Loan, 30 year term. 4% interest = $3,758 per month Principal & Interest = $45,096 pa
Commercial Loan, 10 year term. 6% interest = $2,721 per month Principal & Interest = $32,652 pa

Total loan repayments = $77,748 pa

The $140,000 nett profit after loan repayments of $77,748 leaves $62,252 annual free cashflow.

In 10 years time, approximately $365,000 will have been paid off the original $805,000 total loan principal, leaving a debt of $440,000.

Summary: 10 year nett Manager earnings of $622,520 plus debt repayment of $365,000 = $987,520, which is $98,752 per annum on average. Keep in mind this is clear after the Manager's housing costs.

Disclaimer:
The loan and business trading examples above are provided strictly for illustrative purposes and should not be taken as any type of financial advice. Varying profits, interest rates, loan-to-value ratios (LVR) and loan principal amounts will all vary the results. Potential purchasers should conduct their own investigations and seek qualified financial advice.

Is this "buying yourself a job"?

You could look at it that way, but it's also buying yourself a home, often in a premium location.

In the example we've given, the owner of a $1,190,000 MLR could make $62,252 per annum clear and that's after mortgage repayments. The Manager is also reducing debt by an average of $36,500 per annum over 10 years. A "real job" would have to pay very handsomely to be able to completely cover home mortgage payments, reduce debt and still deliver a $62,252 surplus.

Are there any licensing requirements?

Yes. In NSW, operators of Management Letting Rights Schemes require a NSW Real Estate Agents License. Certificate IV courses can be completed online. In some cases, the Manager will also handle sales of apartments in the complex, providing an additional income stream. This is possible using the same licence and is easily handled considering the Manager lives onsite.

Can the Manager live offsite?

Yes - in some cases this may be practical or preferred, however check the Agreements to be sure this is possible.

What are the risks?

Like any business, it's important to identify and then avoid or manage risk.

We've outlined a few common scenarios here.

1. In a Management Rights scheme, apartment owners appoint the Onsite Manager to market and rent their unit. In some schemes, apartment owners have other options such as Off-site Management (by a local real estate agent), or even Self-Management (perhaps using Stayz or AirBnB). There is a risk of one or more apartment owners opting out of your management service. Keep in mind it's hard to beat onsite management for convenience – owners would not only need to handle their own marketing, they'd need to arrange keys; deal with problems for guests; arrange their own cleaning and maintenance services. The other challenge of self-management is missing out on "walk-ins" and group bookings. We've seen plenty of examples of unit owners leaving the letting pool, only to come back in one or two months. This is normally not a substantial risk as you can generally accommodate the same number of bookings with fewer apartments – it just means higher occupancy and income for the remaining owners.

2. Some schemes allow unit owners to reside in their property, or to rent it out permanently. In that case, such owners may remove their unit from your management. This is rare in "Holiday" Agreements, as permanent occupancy is not permitted. You can check the type of occupancy that is permitted on the DA Approval, or it may be noted in the scheme Agreements.

3. In the case of very poor performance, the owners committee may have the power to terminate and replace the Manager. This is fairly extreme, but can happen if relationships have soured.

4. General risks of a downturn in trade – 2020 has certainly highlighted this risk, although we remind buyers to assess the true value of an MLR business over at least 3 years.

What are the advantages of this type of business?

- Living in a premium location, which might otherwise be unaffordable
- Generally limited hours of operation (morning and afternoon)
- A profitable business to easily replace your income, and more
- One partner often still has a "real job" and can have a proper office to WFH
- The flexibility to live where you work; no commuting
- Being your own boss

How do Managers earn income and can this be improved?

Managers generally receive a commission for achieved revenue, this will be set out in the Management Agreement. A quality manager who improves occupancy and/or room rates will achieve higher commission revenue.

The Caretaker Agreement generally sets out a salary for prescribed duties maintaining the complex – often this will be limited to lawnmowing, light gardening and cleaning the pool. The Manager receives an annual salary for these duties, which is certainly a great base income.

Managers also often charge fees for cleaning apartments (housekeeping), as well as arranging tradesperson maintenance.

A Manager who is achieving strong results for their owners will likely attract additional units into the letting pool, meaning more rooms to sell and potential for more commission and fees to be earned.

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Top Tips

Management Letting Rights (MLR)

1. Management Letting Rights (MLR) may well provide the ultimate "Working From Home" lifestyle.
2. Assess your suitability to the industry and look for a premium location where you'll enjoy living.
3. Each MLR scheme is different, so be sure to fully understand the Agreements.
4. Always carefully review financial reports.
5. Check and compare the asking price for the Real Estate Value in the local market.
6. Talk to your finance broker about what you can afford, plus available loans and funding options.
7. Call or e'mail Tourism Property to discuss what might work for you, or with any questions.

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Dictionary

Management Letting Rights (MLR)

Multiplier
Measure of yield, or return on investment for the Business Value. Generally between 2.5 and 6. Expressed as “3 times”.

Business Value
Nett profit including Caretakers Salary, multiplied by the Multiplier.

Real Estate Value
Total market value of Managers real estate on title; including apartment, garage, office, storage, perhaps café or function space. Often an appraisal by a local real estate agent is available.

Loan-to-Value Ratio (LVR)
Financial lending term - percentage of debt compared to the Real Estate or Business value. Often expressed as “65% LVR”.

Management Letting Rights (MLR)
Scheme appointing a qualified Manager to live onsite and in an apartment complex and operate a letting business. Usually includes a Caretaking component for which a salary is paid.

Management Agreement
Document setting out rules, requirements and expectations between the Manager and the Owners Corporation, or Committee.

Caretaking Agreement
Document setting out the Caretaker’s duties and Salary for general maintenance of the Common Property.

Caretaker Salary
Amount noted in the Caretaking Agreement for performance of the Caretaker duties. Often linked to CPI for annual increases.

Manager
Person or business appointed to operate the Management Rights Scheme. Normally also the Caretaker.

This Explainer contains examples for illustrative purposes, opinions and general explanations, however nothing in this Explainer can be construed as financial advice. Potential purchasers should satisfy themselves as to the accuracy of information and should seek professional advice as needed.

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