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Stephen and Henry are Principals in Global Golf Advisors which Stephen launched in 1992. The Toronto-based firm is the largest advisory firm in the world specializing in golf-related businesses and a friend to NGCOA Canada. For more information, visit www.globalgolfadvisors.com.



10 Steps to Maximize the Value of Your Business **Exit Strategies**



Golf courses are purchased or built for many reasons. For some, they are an inheritance, for others, it is part of a real estate development. In Canada, most courses are owned as stand-alone businesses and were acquired to produce income and become a long-term investment.

TOP 10 CONSIDERATIONS

Over the past decade the economy has slowed, the number of golfers has remained constant, and competition has created lower average green fee rates at most courses. All of the above has created lower operating income and reduced golf course values. So what is your exit strategy?

In order to develop the appropriate exit strategy and maximize your ultimate return on investment, here are the 10 things you should know and understand about your golf course investment:

1) Why should a golf course owner plan an exit strategy?

Each owner typically acquires a golf course with a short-term goal; be it 'lifestyle' ("I have always wanted to own and operate a golf course"); or, over time the land will increase in value and potentially be sold as either a golf course or development land. For some, the golf course was built to support a real estate development and enhance the value of the lots and absorption rates for

sale of lots. Whatever the reason for acquisition, it is essential that any investment focus on both the short and long-term.

If the owner does not understand their exit options and the impact to ultimate value, they may make decisions during the ownership period that reduce the ultimate exit value or the potential to meet their long-term goal. For example, a real estate developer wants to control the golf course during the sale of lots and homes, but typically does not want to own and operate a golf course after development. However, a family-owned course owner may want to pass the course from one generation to the next while protecting ultimate value.

2) What are the components of a reliable exit strategy?

The key components should ultimately improve value and ensure that the ultimate end-goal can be achieved with minimal tax exposure and maintain some flexibility regarding disposition. As such, the following components should be considered:

a) If this is a family asset, have I considered all possible strategies to ensure minimal tax on transfer to my spouse or children? This will require estate planning and potential life insurance policies in order to pay taxes upon death. (Property is deemed to be disposed at fair market value upon death.)

b) How can one maximize the value of the property? Since golf courses typically have significant landmasses with potential development value, all owners should hire a land planner who will ensure that the property rights are protected and the land is considered for future zoning changes. The planners will also help review the property for any internal development opportunities and evaluate any opportunistic land acquisitions that should be considered as neighbouring properties come up for sale, if applicable

c) What is the intended lifecycle of the investment? Evaluate lifestyle and determine whether this is a 5-year ownership or a 30-year plus ownership. In addition, determine whether you want to own the course during retirement years or sell prior to retirement.

d) What do the savvy owners do? Based upon the intended life cycle of the investment, they develop a business plan that considers capital maintenance of assets and enhances operating income before ultimate sale. The plan should always consider the need for flexibility as circumstances change.

"Many golf courses throughout North America are being targeted for future residential and mixed-use development."



3) What are the options for selling your golf course?

For golf course owners who are ready to either cash out their golf course investment or wish to exit for other reasons, there are several options for selling your course. One can sell the course outright, repurpose the property for highest and best use, or disassemble the property and sell the assets on the premise that the sum of the parts has greater value than the sum of the whole.

First, your golf course is worth a multiple of the trailing twelve months' cash flow from the operation. The cash flow of the business is the cornerstone to market value. Some buyers want to discount market value by taking allowances for capital expense replacements – usually 3% to 5% of gross revenue – and management, usually 3 to 4% deduction. Beware of this 6% to 9% reduction in property value. The cash flow of the golf course is called EBITDA, which means earnings before interest, taxes, depreciation, and amortization. For easy calculation, a 10% capitalization rate, which is in the current range for golf course transactions, suggests that every \$100,000 of cash flow is worth \$1 million to the golf course owner (seller). Without cash flow, the fair market value of the golf course is de minimus.

Some buyers are acquiring golf courses on the basis of a 1.25% (average) multiple on gross revenue. For privately held and family-owned golf courses, this approach spares everyone the tax-motivated expenses that are not direct costs of the operation.

Knowledgeable golf course buyers currently adhere to the following shortlist of requirements in selecting acquisition targets:

a) Course is located in or near a primary metropolitan market.

b) Proven positive cash flow is evident.

c) Current debt is within the accepted standard (manageable).

d) No litigation, unpaid taxes, or catastrophic claims are pending.

e) Deferred care and upkeep is not extreme.

Second, what is the highest and best use for your property? Should it remain a golf course or can you consider repurposing the use of the property to market demand? For many older golf courses, lacking deed restrictions that may limit property use and entitlement, there are many options. Often the value of the underlying land is greater than the commercial value of the golf course, based on fair market value as calculated by multiples on revenues or EBITDA. Be prepared to provide a prospective buyer with audited financials to prove your cash flow representations.

If your golf course property is unrestricted by deed or entitlements, you are well advised to conduct a property valuation that can estimate the fair market value of the property for various uses. This step does not require an MAI appraisal, as an estimation of value is enough for directional guidance. Talk with real estate professionals/land planners and study the current and emerging uses for land in and around your location. Like most other categories, land value follows relatively predictable cycles. Learn what the highest and best use is for the land beneath your golf course.

Many golf courses throughout North America are being targeted for future residential and mixed-use development. The process that is followed in securing a potential buyer for the property requires, first, that you can validate that there are no restrictions for developing the course for other uses. Next, buyers require that the course property pass all environmental regulations by way of a simple environmental analysis and audit. Sophisticated land developers and builders will move quickly if they wish to lock-up your property, and extremely slowly if they are under-capitalized or not prepared to move forward due to market conditions. Each behaviour is an indicator of the risk to the golf course owner.

Next, understand all of the assets possessed as a part of the golf course enterprise. Many golf course owners forget the value of the following assets and categories:

a) Have you determined the fair-market value of your inventories (such as petroleum, chemicals, and fertilizers).

b) What is the street value for your rolling stock, to include golf cars and turf maintenance equipment?

c) Are there other assets or resources, such as mailing lists and best management practices, which may have market value if you are at liberty to sell them?

It is sometimes a beneficial strategy to disaggregate the assets provided that the remaining liabilities can be eliminated by the proceeds generated by the sale of the assets.

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4) How does one calculate fair market value of your course?

For the most part, stand-alone golf courses are valued based upon discounted cash flow. The discounted cash flow is based upon the highest and best use as a golf course. For example, if your course was a private club and broke even, each year the discounted cash flow would be based upon the Club being operated to make money and would be examined as a 'pay for play' course.

The discount rates used to calculate value are based upon the risk of achieving projected results and interest rates at the time of sale. As a result, a golf course with consistent operating cash flow has a more predictable cash flow; and as a result, the interest rates regarding the future return on investment will be lower. This provides a lower capitalization rate of around 10% to 12% or a multiple of cash flow after deducting a cost for capital maintenance (benchmark: 3% to 5% of gross revenue) of 9 to 10 times.

If the operating results are based upon projections, the risk of realizing the results is much higher, resulting in a higher interest rate and a lower multiple of cash flow.

In the current investment environment, cash flow multiples range from 9 to 5 times operating cash flow after capital maintenance with historical or trailing cash flow having the higher multiple and projection having the lower multiple.

The value of the golf course is also determined based upon alternative uses (development) and will be determined based upon the risk of development, the number of development acres, and current real estate values in your location. The bottom line is to always maximize operating cash flow in order to enhance value and protect your land rights for ultimate use.

5) When is the best time to sell a golf course?

This question naturally depends upon your exit goal; however, this discussion will only consider optimum time to sell. Based upon your existing use of the golf course, the optimum time will be dependent upon the original reason for ownership of the golf course.

From a developer's perspective, the best time to sell would be when the majority of lots – usually at the 80% absorption level – have been sold and the revenue for the golf course may have been maximized from selling mandatory memberships to homeowners. In this situation, the developer's control of services has maximized lot sales and operating income is very predictable. These two factors maximize cash flow and ensure a higher value.

From an owner/manager perspective, the best time to sell will be at the point in time where operating cash flow has been achieved or the property has been approved for



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re-zoning and development use. The key to maximizing revenue will be a detailed market analysis and marketing plan that analyzes the various markets to optimize yield management, green fee, and cart revenue potential.

Once the cash flow from operations has been optimized, the best time to sell will be when the economy improves and there are potentially multiple buyers. However, based upon the current economy with low interest rates, an upturn in the economy may cause higher interest rates. As such, the opportunity to leverage the return on investment through a debt purchase will be reduced and value will be negatively impacted.

As such, the ideal time to sell a golf course in today's economy will be at the point in time when cash flow is maximized and the economy is showing signs of recovery. In Canada, most golf course transactions occur in the late summer or early fall. Who wants to own a golf course during the winter?

6) How does one increase the value of his or her golf course?

Typically, most owners have evaluated operating costs, almost to the detriment to the golf course quality and service. Expense areas that must be evaluated are operating leases for golf carts and maintenance equipment. Obtain three competitive bids and do not accept employer favourites, as this may cause higher equipment costs and lease rates, which reduce golf course values.

The future value comes from optimizing revenue: green fees, member dues and cart revenue. As such, a detailed market analysis needs to be completed in conjunction with a yield management analysis and focused marketing program.

Too many operators get caught up in believing that each tee time has the same value to the market. The value of each round is dependent on the market and what patrons want to play. Setting the highest rate that a patron will pay is not discounting, and owners should focus on using the best method to let patrons know of their inventory value. Results are key – selling appropriately priced rounds is the solution. A good rule of thumb is to sell the worst tee times first. The most attractive tee times tend to sell themselves.

Selling cart rounds is also a function of selling more rounds. Selling more rounds will optimize all revenue including food and beverage merchandise; however, typically only 20% to 25% of these sales impact cash flow. The keys to increasing the value of your golf course are branding, creating market differentiation, and delivering a golf experience that is 'Best in Class' compared to your competition.

A golf course that is playable and meets the expectations of patrons has the potential to outperform the competition. As such, a focus on marketing, with social media and a strong yield management program, will maximize cash flow and the course's reputation in the market place.

If the golf course is part of a residential community, it will be important to develop a program that either guarantees a monthly fee from homeowners, or enhances the opportunity for residential participation. Remember that value is increased as operating cash flow is improved.

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7) Where should one look for a buyer?

There are numerous companies and individuals who are prospective buyers of your course. Ask people who you know and trust for introductions to proven golf course buyers; there is a small group of business professionals, such as chartered accountants, lawyers, club managers, golf professionals, and experts in professional firms who are familiar with prospective buyers. Do your homework!

Do not waste your time on unproven or unknown buyers. The NGCOA Canada is a valuable clearing-house for known and trustworthy buyers. When you receive leads or introductions, investigate the background and history of the prospective buyers. Ask around. The questions to which one needs answers when selling a golf course are:

a) Have you ever purchased a golf course previously? If “yes”, which ones?

b) Who were the owners with whom you worked on those deals?

c) What is the process that you typically follow when acquiring a privately held course?

d) Will you execute a nondisclosure and confidentiality agreement with me?

e) What information do you need in order to formulate your offer?

f) What is your timeline for closing in the event that we get to that point?

g) When I call Stephen Johnston at Global Golf Advisors in Toronto, will he know you?

h) What is your source of funds for this acquisition?

i) Do you contemplate using debt for all or any part of our deal? Is the debt portion pre-arranged or will our deal be contingent on arranging for a purchase loan?

“Do not waste your time on unproven or unknown buyers. When you receive leads or introductions, investigate the background and history of the prospective buyers.”



j) Do you require contingencies when you acquire golf courses? Or, will you make me a clean and unfettered offer?

8) What are the typical terms and conditions of a golf course sale?

Typically terms and conditions are unique to each course, its owner, and the potential buyer. Price, payment terms, and closing date are always addressed. Each transaction had characteristics that demonstrate the wants and needs of the respective buyer and seller.

9) Is there such a thing as a standard golf course purchase and sale agreement?

Most golf course purchase and sale agreements follow a similar pattern but there is not a ‘form’ agreement one should follow. Spend the money to engage professional guidance and resist the urge to cut and paste your own agreement.

Regardless of your success in other asset categories, secure legal guidance from a lawyer experienced in buying and selling golf courses.

Most experienced buyers will offer their own agreement. Keep in mind that the trade-off in using the buyer’s agreement you are choosing to make the transaction a “home game” for the buyer! Expect the agreement to address the following characteristics:

a) Property Description: What are the metes and bounds of the property? You will be surprised at the informality of long-standing property boundaries.

b) Standard Terms: Typically there is a section that describes the parties and their authority to engage in such a contract and their baseline understandings. If certain assets are not to be sold and will be removed from the property before closing, these assets should be identified.

c) Purchase Price: The best deals have simple price considerations with few contingencies.

d) Contingent Considerations: Usually golf course transactions have contingencies, such as securing adequate funding, confirming environmental satisfaction, and allowing for certain capital investments that may be deducted from the purchase price.

e) Broker Fees: If a broker has helped to facilitate the transaction, one must document the obligation to pay the broker on closing.

f) Due Diligence Period: For what period of time must the course be ‘off market’ while the prospective buyer is confirming the asset characteristics and condition?

g) Employees: Most purchasers will not want the severance liability of long-term employees. As a result, they may want the owner to release the employees so that the buyer has the option to re-hire with no historical severance liability.

h) Closing Date: When does the property change ownership?

This short list has many additional elements that a capable lawyer will coordinate for you. Be diligent and patient. Establish clear-cut understandings and live up to your commitments while expecting the same of the buyer.

10) How does one forecast and anticipate the tax ramifications in selling a golf course?

In Canada there are various opportunities to reduce tax on sale, especially through the sale of shares or capital gains deductions. Prior to purchasing a golf course or developing the appropriate strategic exit plan, it is essential that a tax expert be consulted in order to appropriately set up the correct corporate structure that will meet your goals and objectives. The key will be to maximize deductions and optimize capital gain exemptions.

It is essential to honour the requirements of Canada Revenue Agency in all matters. At the time of sale, a tax advisor is again required in order to give the appropriate advice, as purchasers typically will want to acquire assets and not shares in a corporation. As a seller, one needs to know all the various tax issues in order to

develop an appropriate sale document. The sale document will be essential in Canada Revenue Agency accepting your tax filing, as this document is ‘third party evidence’. It is very difficult to defend a filing after the sale if the purchase and sale document does not support your ultimate tax filing upon disposition. So, plan ahead.

MAXIMIZE YOUR INVESTMENT VALUE

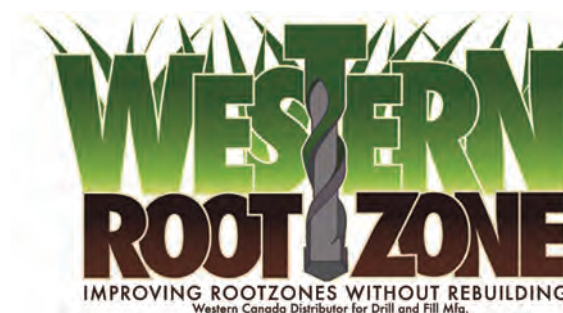
In summary, your exit strategy should be planned at the time of purchasing your property. If you do not have an exit strategy, now is the time to develop one. The best plans identify the reason for acquiring the golf course and the expected return on investment. Whatever the reason for owning a golf course, it is important to develop your operating strategy that meets the goals of your exit strategy.

A well-known, well-operated golf course gains notoriety and a golf course that consistently maximizes cash flow, gains in value. Typically, a golf property with strong cash flow can re-invest in itself and stand out among its competition, with players patronizing the golf courses.

A course with a great brand and positive cash flow increases value at the time of sale and gains a superior value due to multiple bidders. As with most businesses, a strong marketing and business plan are essential ingredients to maximizing investment value and allowing the owner greater flexibility as to when they want to sell. Without an exit plan, it is likely that you will not maximize your investment value.



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