# SALE LEASEBACKS
## A Franchise Owner Parachute

**By: Teal Henderson**

Both investor appetite and seller tenant necessity sparked an uptick of sale leaseback activity in 2010. A growing number of franchisees exercised this option for the first time since 2007 in addition to corporate-owned entities as a parachute to continue operations. Sale-leasebacks also supported overall growth, stockpiling equity and restructuring existing debt. Fortune 500 companies sold regional and national headquarters. Industrial conglomerates sold large distribution centers and portfolios of assets, respectively. Municipalities sought to lower deficits and balance budgets with government service assets by heading to the sale leaseback table.

Perhaps, the sector best realizing the value added with sale leasebacks were single and multi- unit franchise owners. Real estate could be a large portion of a franchisee's equity investment and it may ultimately hinder their growth strategy. With lenders not availing themselves as regularly to operators with smaller balance sheets, then a monetization of the real estate currently in place could be an alternative solution option.

Since the economic downturn hit all sectors, many single and multi unit franchise owners found themselves facing closures and dissolution. Property ownership was no longer viable to the current business plan. Sale leasebacks have given extended life to the franchisees needing immediate capital, flexibility and time to ride out the constriction or leap on sale priced expansion assets.

In 2010, sale leasebacks were used frequently by franchise owners for alternative financing vehicles to fund new store openings, maintain operation of current stores or invest in core businesses. During peak market conditions from 2005 – 2007, franchise sale leasebacks were some of the most coveted assets for investors. However, during the downturn, some were merely in a survival mode using equity to fund payroll and maintain inventory. The ability to redeploy otherwise illiquid assets was and is key for many franchisee's survival and for others a well-timed growth and expansion opportunity. Multi-unit owners eliminated property ownership to simplify accounting and negate cross funding between stores with varied levels of sales and success and ownership structures.

**Let's look at some of the franchise considerations and points of interest when contemplating a sale leaseback:**

- » Ability for immediate cash infusion for operations
- » Use of equity for growth and expansion
- » Continuity and uninterrupted operations and control of property
- » Increase financial flexibility with creation of self financing and risk allocation
- » Loss of depreciation but gain lease payment deductions- proper structure of lease
- » Some seller tenants have depleted their depreciation of property and thus there is less tangible and accounting benefit for retaining property
- » Allows for restructuring, improving and simplifying balance sheets
- » Bargaining opportunity for owner on lease options: buybacks, renewals, go dark options, assignments etc
- » Preparation for a timed exit
- » Ability for multi unit owners to sell numerous assets as a portfolio and negate multiple transaction fees
- » Lowering costs with rent payments possibly lower than mortgage payments

There are numerous factors for franchise owners to consider with regard to transacting a sale leaseback, including the tax basis and possible penalties, corporate requirements and personal guaranties potentially necessary to close the deal. Proper lease structuring is key to the longevity of the site as well as creating a salient asset for the ultimate NNN lease investor/buyer. ■

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