Chapter 5: Asset Valuation (Real Estate)

Real estate may be the largest fixed asset on the balance sheet. The two most important items to consider are either the market value of the building if it is part of the transaction, or the lease if the building is not part of the transaction.

Introduction

When valuing a gas station and reviewing the real estate component, you need to look at one of three things, depending upon whether the seller owns the facilities or leases:

(1) The value of the facility (if the seller owns the building/buildings).

(2) The value and duration of the lease (if the seller does not own the building).

(3) Some combination of the two (if the facility will be leased by the seller, then the fair rental rate should be determined).

The lease and real estate facilities of a gas station are the most important items to review before valuing or purchasing a gas station. It is critical to know how much land there is, how much building space there is, where is it, whether the property is owned or leased, and whether it is for a market value or a liquidation value. The building and land characteristics of the property, as well as its market supply and demand should be accurately determined.

Valuing a Gas Station’s Real Estate Assets

Valuation Example

The best way to understand real estate valuation is through the use of an example. Throughout this chapter, we will present a quick valuation of a gas station/convenience store. This analysis will assist the reader in understanding how this asset fits into the overall business valuation. Many steps have been skipped, but the issues and analysis will give a buyer/seller or analyst a good “back of the envelope" indication. The most important specifics of this building can be seen in Table 5-1.

Table 5-1: Land/Improvement Statistics of an Example Gas Station

Item	Statistic
Location	Southern California
Interest Valued:	Fee Simple
Land Size and Shape:	35,082 square feet / rectangular
Zoning	C1, General Commercial
Gross Building Area:	3,167 square feet
Year Built	1987
Effective Age:	19 years
Construction Type	Structural Steel / Concrete
Number of Pump Islands	8
Parking	15 spaces
Amenities	Restrooms/Convenience Store

Before reviewing the different techniques of valuing a gas station or a building, it is important to understand the various ownership interests in real estate, as well as the critical and unique building and land statistics.

Ownership Interests

There are four general interests in real estate:

(1) fee simple
(2) leased fee
(3) leasehold
(4) partial interest

Fee simple interests are the most common, meaning that the property is not encumbered by any other interest or lease. This interest is most used when valuing an owner user property where there are no tenants, and the owner (seller) also owns both the land and building.

A leased fee interest means an ownership interest held by a landlord, but leased to others; the rights of the lessor (landlord) or the leased fee owner and leased fee are specified by contract terms contained within the lease. This interest is involved mostly when valuing income producing property with leases such as industrial, office buildings or retail centers.

A leasehold interest is defined as the right to use and occupy real estate for a stated term and under certain conditions, conveyed by a lease. This interest is generally involved when valuing a land lease or the lease of a tenant.

Finally, a fractional interest is an interest in either of the three interests seen above but is less than 100%. An example of this would be a house in which three people have one-third interests.

Table 5-2: Important Land Characteristics

Item	Description/Comments
Location:	Get the address (look at title report/tax bill)
Assessor's Parcel Number:	Needed to establish basic tax identification and other statistics. Generally found on the tax bill.
Size and Shape:	There are 43,560 sq ft in one acre. This is a critical factor since you need to know if there is enough room for expansion, if your parking is less than the overall market, or if there is excess land which is an additional asset for the balance sheet.
Ingress/Egress and Exposure:	If you cannot access the property, or are subject to a short term easement, then the value is much lower.
Adjacent Properties:	Is the property next to other retailers?
Topography:	Are there problems here? A hard rain or earthquake may make a building slide down a hill. Some buildings gradually shift down a slope.
Drainage and Storm Water Control:	Will the building float away? You may need flood insurance.
Hazards:	What was the building previously used for? Is it on top of a fault line (earthquake)? Is it contaminated by toxins (lead, methane)?
Easements, Restrictions, and Encroachments:	Does the title report flag any issues? The seller may not even know about these, such as the right for a neighbor to drive across your property.
Utilities:	Will you have to dig a ditch for sewage, water, or electricity, and pay for two miles of digging and engineering to make the building operational?
Zoning Provisions:	This is a big one. It is absolutely critical to find the existing zoning code. If your building burns down can you re-build the same structure? In most cases you can't. Check to see if you need a conditional use permit (CUP) for your business.
CC&Rs/Private Restrictions, Governing Use:	Nail these down. These usually appear in the title policy and show any restrictions on the use of the property.
Tax and Assessment Data:	Are you being over-assessed or under-assessed? Also, you want to find out when the next assessment is for the county. Your taxes may double.

General Land and Building Analysis

Before valuing anything, one must know the gasoline station and/or C-store building and land parcel sizes. First, the site improvements need to be reviewed. The general characteristics for a land parcel can be seen in Table 5-2 on page 119. Critical improvement characteristics are seen in Table 5-3 listed below.

Table 5-3: Important Gasoline Station Characteristics

Item	Comments
Gross Building Area:	Get the correct square footage.
Exterior:	Concrete, wood?
Foundation:	Is it flat?
Roof:	Do you need a new one? This can be expensive! How old is it?
Air-conditioning/Heating:	Same as the roof.
Plumbing:	Do you need new plumbing? Is there sufficient plumbing for restrooms? Are there plumbing and drains available for multiple concessions stands?
Fire System:	Will the fire department allow you to operate in the existing facility as a gas station?
Parking:	How many spaces are there?
Environmental:	Asbestos, etc.? Are you purchasing an off balance sheet liability?
Age:	Is the building about to fall over, or has it been maintained?
Functional Obsolescence:	Are there problems with the building which impact the operation of the business? For example, if you are to lease or buy a building and there is no air conditioning system, then this is a problem.
Deferred Maintenance:	This is critical. You want to know going into a deal whether you need to pull out your checkbook for a new roof, electrical wiring, earthquake retrofitting, asbestos abatement, plumbing etc. Get a good structural engineer and contractor when in doubt (even when not in doubt).
Signage:	Are there signage posts with good exposure to traffic? Can the station be clearly seen from a free-way?
Amenities	What extra services are provided?
Capital Expenditure:	What is the most recent capital expenditure? Any future expenditures?

Market Analysis

The analyst should then determine the vacancy rates in the area, the amount of space which is being built or planned, and whether vacancy rates and rental rates are decreasing or increasing as a result of supply and demand imbalances. This information may be obtained from real estate brokers or from appraisers. Also, contact the city planning department for additional information on future development. One should not get into a long term lease, only to learn that better and new space is about to be built, or a competitor is about to locate next to you.

You can get much of this information on-line from commercial real estate brokerage companies. These companies and their respective web sites can be seen in Table 5-4.

Table 5-4: Market Analysis Sources

Commercial Real Estate Company	Web Site
CB Richard Ellis	http://www.cbrichardellis.com
Cushman & Wakefield	http://www.cushmanwakefield.com
Marcus & Millichap	http://www.marcusmillichap.com

Different Types of Gas Stations

Within the USA and Canada, gas stations are generally broken down into three categories; (1) premium branded gasoline stations and convenience stores; (2) discount brand gasoline stations; and (3) high volume retailers.

Premium Brand Gasoline

Premium brand gas stations sell well recognized, leading brand gasoline such as ExxonMobil, Shell, BP or Texaco. They usually have fully automated Pay at Pump technology, allowing for the ease and convenience of paying at the pump rather than having to purchase the gasoline instore. Many of these premium brands provide their own credit cards for the purchase of fuel.

Usually, the price of premium brand gasoline is higher than that of discount brand gasoline. Premium brands often have little control over the price they can charge for their gasoline products as they are fixed to one supplier. Premium stations have many more locations throughout the country compared to discount brands. They occupy much larger spaces and more versatile locations, and therefore have many more pumps available per gas station. Premium stations usually offer additional services such as vehicle maintenance, repairs or convenience stores. In addition, toilet facilities are usually available in premium stations. Premium gasoline stations are generally much cleaner, more modern and brighter than discount brand stations. They are usually extremely visible from the highways with very tall signs used to display the brand logo.

Convenience Stores and Co-branding

The most recent change in the gasoline industry occurred in the 1990's; the increase in C-stores. In order to increase gasoline sales and profit margins, major oil companies installed their premium brand stations with convenience stores. These stores were located in strategic locations, such as major highways, to maximize sales. "Co-branding" came as the convenience store expanded throughout the gasoline industry. Two or more franchises were paired together under one roof, which brought benefits to both the franchisees and the customers. Fast food outlets such as Burger King and McDonalds have become popular co-branders with gasoline stations. These additional services were introduced in