Instructions for Using the PrimusREIT Database to Determine the Discount for Lack of Control

The PrimusREIT Database is contained within the PrimusPVX valuation application. While PVX is designed to provide comprehensive support for valuing all types of fractional interests in real estate, it is also possible for the valuer to make use of its parts to support other valuation methodologies. These instructions apply for valuers who wish to obtain a discount for lack of control (DLOC) for use with their existing models when valuing interests in real estate limited partnerships and LLCs. The PrimusREIT Database can serve as a direct replacement for Partnership Profiles' Public Limited Partnership Secondary Market-based discount and rate of return studies, while the PrimusPVX structure allows you to connect the DLOC to your subject partnership far more precisely than with the former public limited partnership data. In PrimusPVX, you not only have an enduring data source, but you will also have more powerful and credible valuation analysis.

To take advantage of the PrimusREIT Database, you must first create a project using PrimusPVX. If you do not yet know how to do this, please refer to the New User Tutorial in the Resources section. Read on to discover how you can use the model for its DLOC conclusion. As a subscriber to PVX, you also have an online copy of Valuing Fractional Interests in Real Estate 2.0, the only multidisciplinary work on this topic. It includes the entire development and application of the PrimusREIT Database on pages 148–174, which follow the section on Partnership Profiles data. You will find this helpful for switching over or for integrating the two methods in your valuation report.

Drawing specific connections to your partnership

Critical elements specific to your partnership are accommodated in a very general way when you select public limited partnership data (general property type, no/low or mod/high distributions, no/low or mod/high leverage, for example). PVX allows you to be far more specific, using your actual real estate cap rate (net operating income divided by market value) and growth rates that you can get from your real estate appraiser. You are no longer pretending that your partnership faces the same sort of economic conditions as the selected public limited partnerships, you are using its actual asset market returns and growth.

By entering a simplified version of your partnership's balance sheet in the Entity Properties window (including any mortgage loan details and adjustments) you get—instead of a rough "leveraged or not" comparison—your partnership's actual declining loan balance, which can have a big effect on partnership risk and the concluded discount.

In the Control: Management window, you are guided to consider specific challenges faced by your partnership's management and how well you expect them to be addressed in the future. You will make an adjustment based on the specifics of your case. It is helpful to consult with your real estate appraiser on this, since management (specific company) risk can vary from near-zero to really worrisome. The systematic method for doing this is logical, transparent, and a big step up from simply assuming that public limited partnership management is always similar to your partnership.

In the Control: Subject window, you are guided to make an adjustment as you consider rights that may be granted by the operating agreement to your subject interest holder that allow it to reduce risk in ways that a minority shareholder (in either public limited partnerships or listed REITs) cannot.

By following these systematic steps you are actually modifying the DLOC until you end up with a highly specific and supportable minority discount.

The discount for lack of control

Your inputs, answers to questions, internal calculations and conclusions are all provided in your User Valuation Summary (UVS), ready for your report.

Formulas showing the risk premiums that are attributed to control loss (Y_F), management risk (A_{MC}) and subject risk (A_{CR}) are shown along with their solutions at the end of the two Control Properties sections. The calculations to this point are all based on yields, even though you may be looking for the DLOC.

The remaining calculations in the Discounted Cash Flow Model (Valuation Models section) show you exactly how the DLOC (D_C in the UVS, also shown in the Control: Subject window Advanced section) is determined and are suitable for pasting into your report if you wish. You will find the DLOC calculation and a summary of the minority value conclusion at the end of the section. You can use only the DLOC with your existing valuation model, or you can use the yield rate (Y_C from the top of that same section) if you are using an income model. The DLOC substitutes for the Partnership Profiles discount study, and the yield substitutes for the Partnership Profiles Rate of Return Study.

Additional REIT support for your report

In the PrimusPVX Learning Corner (see Resources in top menu), you will find a handy Valuation Report Preparation Guide to assist in writing your valuation report. Included as a supplement to this guide is a sample REIT Market Yield Data Appendix, which can be copied and pasted in full into your own valuation report or its appendix. You'll want to replace the two data tables in the sample appendix with the ones in the REIT Data Tables section of your User Valuation Summary, update the REIT data at the top of p. 2 with the values from the REIT Narrative Data table, and replace the yellow highlights with your own data throughout.)

The underlying REIT data are available upon request for your date of value, should you wish to include it in your valuation report.

Your work for obtaining a DLOC for your partnership valuation is now complete and can be used with your other models for LLC and LP interest valuations. The process for valuing general partnerships or deeded interests in real estate (tenancy in common) is a bit different. You may be able to adapt the DLOC for those interests too, although there are usually substantial differences between these entity types and the normal LLC or LP. You may wish to use the guided process of PrimusPVX for these other entity types to take you through the entire valuation process, including analyzing a partition action if applicable.