

# Private-Equity Golf/Country Club Communities: Issues and Answers

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A private-equity country club community presents a number of interesting appraisal challenges. This article highlights some of the problems presented to appraisers during the valuation of private clubs and communities, including the difficulty of determining the value of the club portion of such a community, the importance of determining the value of club memberships, and the need for local market analysis. Several methods for dealing with these and other issues are suggested.

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**T**he residential portion of a golf course property is similar to any other residential development in that the interest being valued (if fee simple) represents the value of the property in its present condition. This is normally based on absorption estimates, costs of future necessary improvements, and other items normally considered in a subdivision analysis. In many cases this value is enhanced by the club.

The club portion of a property poses a more complex challenge. Some of the more pertinent questions to be answered include:

- Is the club operating in a "stabilized" manner?
- Is the facility being valued or are the equity memberships being valued?
- Where is the club in its sellout of memberships (if not stabilized)?
- If memberships are being valued

what importance does the operation of the club have in the valuation process?

- Is the club being developed purely to sell lots or to stand on its own?

One property appraised by the author was a recently opened, upscale club in Canton, Ohio, with a championship 18-hole golf course designed by world-famous golfer and golf course architect, Jack Nicklaus. The large clubhouse is a converted monastery that was undergoing renovation and included a spa, lodging units, and condominium units in addition to typical country club amenities. Approximately 40% of the available memberships had been sold under varying payment terms as of the appraisal date.

At issue was whether we were analyzing the club's operation or the club's ability to sell memberships. Because the memberships sold had been marketed re-

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cently, the group of members was unlikely to sell them to a private purchaser. Also, because the group of members was less likely to have developed into a cohesive group, the members were likely to have difficulty reaching a consensus of opinion. Therefore, any potential purchaser of the club would only have been able to purchase the portion of the club not owned by the existing members. In this case the developer was also responsible for any operating deficit until the club was turned over to the members. It was then concluded that what would be available to a purchaser was the cash flow from membership sales less the operating deficit. Therefore, the valuation included the following steps:

- An estimate of selling prices of memberships
- The sellout (absorption) time of memberships
- An operating profile for the club during sellout
- A discounting of the resulting cash flows

### **MARKET ANALYSIS**

The market analysis posed the challenge of measuring market depth for an upscale club in a secondary market, the pricing of the residential and club membership products, the time necessary for absorption, the contributory value of the signature golf course architect to both the club and the residential real estate, and the best mix of residential products and price points.

The question of market depth was of primary importance because the property was located in a smaller secondary market and was, by design, an upscale, high-priced, and unique community. An analysis of the income levels of existing members and buyers (we were fortunate to have a development that already had some history) was done to determine income levels of typical buyers. The growth of this income sector was then projected by use of demographics and compared with the subject's market share of homes sold in the applicable price range in the local market. New or planned developments were also considered to measure both the supply and projected supply as well as the potential demand.

Product pricing was evaluated in the same manner as any other development. Market surveys were performed and adjustments were made for quality of product and amenities. In the subject's case the property had two factors that separated it from much of its competition. The golf course was designed by Jack Nicklaus, a native and favorite sports hero of Ohio. The extra-large clubhouse with its spa, lodging units, and condominiums is unique even among the most prestigious clubs, not only because of its unusual (for a clubhouse) architecture (a renovated monastery) but also because of its size and amenity package.

A frequent topic of discussion in the golf course industry is the value of signature architects. Signature architects can include famous golfers such as Nicklaus, Arnold Palmer, Lee Trevino, and Gary Player, or renowned nonplayer architects such as Pete Dye, Robert Trent Jones, Rees Jones, Arthur Hills, Michael Hurdzan, or Tom Fazio. In addition, older courses designed by famous architects of the past like Donald Ross, Alister MacKenzie, and William Flynn create great interest and discussion among golfers. Often, the marquee value of an architect can be transformed into higher membership fees, dues, and use fees as well as the possibility of higher lot prices and more rapid absorption. While this value is sometimes significant and can justify the added cost, the cost differential can be as high as \$1 million or more and can result in a large and unnecessary cost if the market resists the pricing necessary to support it.

At the subject property, membership fees for units sold as of the appraisal date exceeded even the highest priced local competition by as much as 40%. With no support in the local market, we researched other Midwestern markets in which Nicklaus-designed courses had recently been built and found that memberships at these clubs exceeded the local market by similar percentages. We were also able to develop a trend for membership sales that indicated a potential absorption rate for the subject property higher than that of developments without this amenity. At this particular golf course there was a value added that justified the additional cost of a signature architect. By no means, however, is the cost of a signature architect always justified.

re numerous areas where the fees  
ply not support the additional cost  
market is not sophisticated enough  
e the signature architect.

analyzing the residential portion of  
ect, the comparison with other golf  
nities as well as nongolf commu-  
uggested that a premium price was  
ble, partially as a result of the  
s name. This was believed to be  
~d by the "favorite son" status of  
s, but it could also be achievable  
right markets outside of the archi-  
me area. Analysis of the residen-  
s from the other Nicklaus devel-  
s in the Midwest revealed a similar  
n to that already realized at the  
property associated with these  
when compared with competing  
ments.

i result of analysis of similar com-  
s, it was concluded that a mixture  
rent residential products at vary-  
e points was best for the subject  
y. As in many upscale develop-  
the original plan was to develop  
rge, expensive, single-family  
The experience of other devel-  
s indicated that a mix enabling  
oderate income levels to partici-  
ould lessen the required depth of  
at the highest income levels. The  
table of these was another com-  
with a Nicklaus-designed golf  
n Indiana, which had developed  
-ge, single-family units and had  
y those with golf course frontage.  
laming lots had experienced little  
success. The subject property in-  
ted a plan whereby large, single-  
omes were developed along much  
golf course frontage, and more  
itely priced patio homes and  
uses were developed in the pe-  
areas. The analysis of the local  
showed this to be a prudent strat-  
ause it reduced the pressure to  
an unusually large share of the  
market. In areas where the top  
brackets are large enough to sup-  
tire developments, this strategy  
t be necessary; however, the de-  
hics of smaller secondary markets  
uire products aimed at younger  
r slightly lower income levels to  
the performance of a project while  
Zing an upscale image. This strat-  
ices the overall risk of the project

because it puts it within reach of a wider  
segment of the market.

## VALUATION METHODOLOGY

The sales comparison approach can take  
two directions. If the interest being val-  
ued is fee simple, it is a typical analysis  
of comparable property transactions us-  
ing appropriate units of comparison such  
as price per member, gross income mul-  
tiplier, membership dues multiplier,  
membership revenue multiplier, and  
overall capitalization rate. Some tradi-  
tional units such as price per hole or price  
per acre are inappropriate because they  
typically fail to provide a common de-  
nominator, like some of the income-re-  
lated units of comparison. If the interest  
to be valued is to include the worth of re-  
maining memberships, the appraiser is  
valuing a potential purchaser's ability to  
sell those memberships. The two areas of  
interest are then achievable price and  
market absorption time. A comparison of  
similar or competing clubs using nor-  
mally applied adjustment techniques will  
produce a reliable estimate of the value of  
the membership. This analysis requires an  
understanding of the different levels of  
clubs that are truly competitive and the  
amenities that are offered. A combination  
of demographic analysis and sale rates of  
similar or competing facilities, along with  
a supply/demand analysis of clubs in the  
market area, should aid in estimating  
sellout time. These conclusions are then  
carried into the income approach, where  
the discounting procedure is applied and  
combined with an analysis of the club's  
operation.

The sales comparison approach is  
therefore limited with respect to estimat-  
ing the value of some private-equity clubs.  
This type of analysis, however, is a criti-  
cal component in developing supporta-  
ble value conclusions for a private-equity  
club where the interest being valued is  
that of a purchaser's ability to sell  
memberships.

An appraiser may be called upon to  
value a private-equity club as a going  
concern regardless of the membership  
structure. In such cases the sales com-  
parison approach can be more useful, in  
that private clubs have transferred own-  
ership at arm's length in some market  
transactions. Such transactions can be

Year	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Net Income	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Operating Profit	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Depreciation	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Amortization	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Interest Expense	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Interest Income	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Other Income	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Other Expenses	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Income Tax	...	...	...	...	...	...	...	...	...	...	...	...	...	...
Total	...	...	...	...	...	...	...	...	...	...	...	...	...	...

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re operated n- rises as to ho- nalysis when- and best use- e, nongolf u- article focus- ial uses. In sa- operating sty- i by employ- d expenses fi-



of the market, because costs can vary widely based on features and amenities such as automatic or manual irrigation, choice of grassing plan, size and number of bunkers, and cart paths.

### CONCLUSION

A private-equity country/golf club community presents a complex appraisal problem. Are membership interests or the ability of a property to produce net income being valued? Does the club contribute to the value of the surrounding residential property? If so, how much? Which approach is most reliable?

The question of what is being valued is the first to be answered. One may be valuing either membership interests, operating profile, or both. As shown in this article, while the valuation techniques for either are familiar, a keen understanding of what is being valued is essential. The ability to understand a club's position in the marketplace is critical to selecting the correct data to be analyzed and to defining the potential purchasers.

The question is often asked: How much does being on a golf course add to the value of a lot or home? There is no "rule-of-thumb" answer. In many cases, however, significant value can be derived from golf course frontage, and from other amenities such as a signature golf course architect. A signature architect can enhance the value of both a club and the surrounding residential real estate in some cases. These effects can be measured by thorough market research of similar properties and their market positions.

There is no best approach. Typically, each approach depends on data or con-

clusions from the others. Ultimately, most purchasers rely on the income approach or analysis, but the information used to develop this approach must be reliable and must come from the market. This usually means borrowing key data or conclusions from the other approaches.

The key elements to developing a supportable value estimate for a private club are an understanding or accurate evaluation' of the facility, and access to the appropriate data from which to develop the various methods of analysis.

It is also important to remember that golf clubs are management intensive and require a significant amount of personal property such as maintenance equipment; furniture, fixtures, and equipment in the clubhouse; and food, beverage, and merchandise sales. This means that business and personal property value must be considered by any one of several methods. It should be clearly understood that the examples illustrated here combine the valuation of both real and personal property. Those examples in which the value of memberships remaining for sale are included illustrate the value of both real and personal property (including business value). To extract real estate value from this would involve one of the methods discussed here or in previously published articles,' none of which has been widely accepted as the most legitimate approach.

The valuation of a private club and associated community involves many of the methods and techniques with which appraisers are familiar. It also offers a unique look at a growing and fascinating industry that reflects an increasingly popular lifestyle.

1. Laurence A. Hirsh, "Golf Courses-Valuation and Evaluation," *The Appraisal Journal* (January 1991): 38-47.
2. See Hirsh "Golf Courses-Valuation and Evaluation"; Arthur E. Gimmy and Martin E. Benson, *Golf Courses and Country Clubs: A Guide to Appraisal, Market Analysis, Development, and Financing* (Chicago: Appraisal Institute, 1992); and Stephen R. Hughes and Kevin K. Nunnink, "Appraising Golf Courses for Ad Valorem Tax Purposes," *The Appraisal Journal* (October 1993): 611-615.